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BusinessWeek

MAY 9, 1995

A MCGRAW-HILL PUBLICATION

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COMPUTERS
SOFTWARE
BANKING
CHEMICALS
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HEALTH CARE
AGRICULTURE
AUTOS
MACHINERY
ENTERTAINMENT
ENERGY
SECURITIES
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UTILITIES
WHOLESALE
REAL ESTATE
FOOD PROCESSING
TEXTILES
RESTAURANTS
STEEL
COMMUNICATIONS
INSURANCE
PHARMACEUTICALS
DEFENSE

What's ahead for
America's 25 key industries

INDUSTRY

1995

OUTLOOK





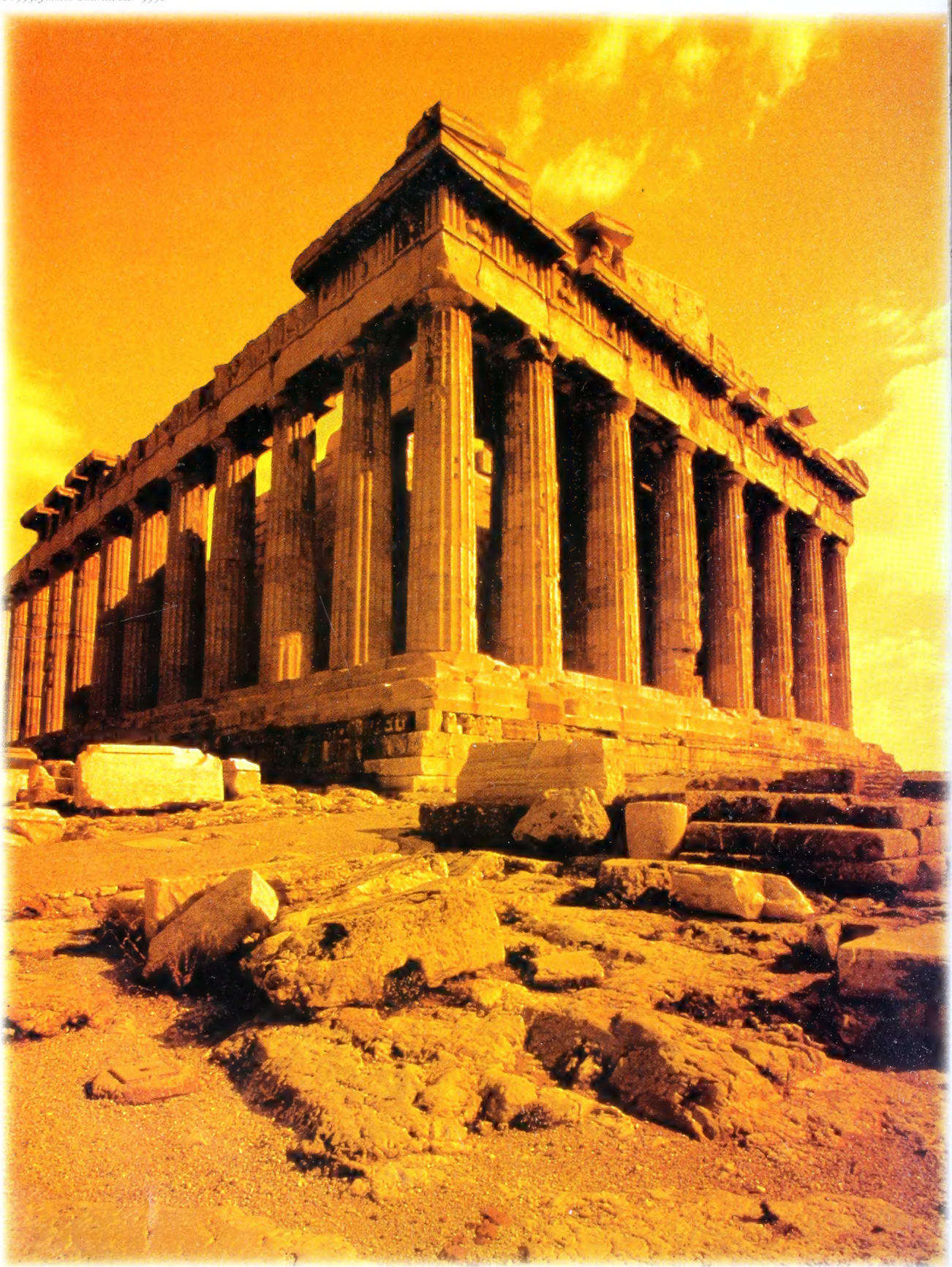
It has a 32-valve, 260-hp engine that takes it from 0-60 nearly a full second faster than last year's model. V8 luxury sedan available. Which means the only place you won't go quickly is your local filling station.

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JOHNSON
CONTROLS

1995 INDUSTRY OUTLOOK

Introduction

54 STEAMING ALONG

It looks like another year of expansion, with exports and capital-goods spending strong and inflation under control

58 SHRINKING THE GOVERNMENT

Downsizing won't hurt the recovery

60 BUSINESS WEEK HARRIS POLL

The top brass is gung-ho for '95

Manufacturing

63 AUTOS

Barreling down a rugged road

64 DEFENSE

Washington won't gallop to the rescue

65 MACHINERY

Demand is creating a deafening din

68 STEEL

Can anything dent this industry?

69 CHEMICALS

A cauldron brimming with profit.

72 FOOD PROCESSING

Its new recipe is proving pretty tasty

High Technology

75 COMPUTERS

If it computes, it's gonna sell

76 SOFTWARE

It's still where the action is

77 SEMICONDUCTORS

The I-Way "will be paved with silicon"

78 TELECOMMUNICATIONS

Talk about dialing for dollars

79 PHARMACEUTICALS

The field is crowded. Pipelines aren't

Natural Resources

81 ENERGY

This year looks like a gusher

82 AGRICULTURE

Full granaries don't mean full pockets

83 FOREST PRODUCTS

The paper recovery isn't pulp fiction

Services

85 HEALTH CARE

Slaying "the beast of medical inflation"

86 RETAILING

Steady traffic at the mall

87 WHOLESALING

The middlemen stay on the march

88 TRANSPORTATION

Airlines can unfasten their safety belts

89 RESTAURANTS

As costs rise, is it bye-bye to fat times?

90 UTILITIES

Suddenly, the juice is switched on

91 ENTERTAINMENT

The battle for the couch potato

Finance

93 BANKING

A delicate balance at the bank

94 INSURANCE

Fields of green—and disaster areas

95 SECURITIES

On Wall Street: This too shall pass

98 REAL ESTATE/CONSTRUCTION

Back from the land of the living dead



CLASS ACTS

Take a bow, everybody:

BUSINESS WEEK picks the top managers, entrepreneurs, and products of 1994 page 101



DY HEAT

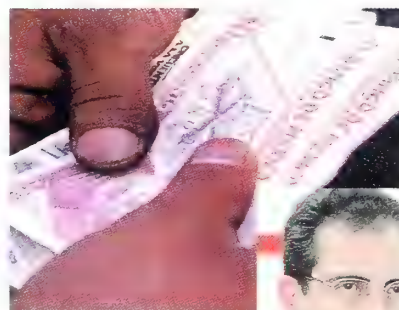
ed's revamped Taurus: Beneath a sleek exterior, it's one complicated machine page 41



MILKEN VS. CANCER

The millions he's pouring into biotech are galvanizing—and vexing—the industry

page 36



PESO PANIC

Devaluation may be a boon in the long run, but Zedillo's ineptness has clobbered investor confidence page 34



ews: Analysis & Commentary

ELTDOWN IN MEXICO

edillo has learned a painful lesson about the market's revenge. Now, can he lead the country bounce back?

MILKEN MONEY

Michael Milken isn't the first rich cancer patient turned research patron. But his latest wealth raises hopes—and concerns

HERE A CUT, THERE A CUT...

Some fairly radical tax plans are out there, but a budget-buster is unlikely

COMMENTARY

Of all the tax-reform proposals, only a few at tax really addresses the issues

AN THE GOP STOP MEGA-VERDICTS?

The party wants to limit legal awards, but it's far from united

"TENSION AND TAUTNESS" AT FORD

Will the new Taurus and Sable rake in the bucks to justify a painful gestation?

WILL THE PC PARTY WELCOME BOB?

Microsoft's new "social interface" sure is friendly—but it's no sure thing

ED ALERT AT FIRST ALERT

faces a PR disaster over its highly sensitive carbon monoxide detectors

46 NETWORK NEOPHYTES

Paramount's and Warner's TV launches will be at less than warp speed

47 IN BUSINESS THIS WEEK

ITT's Araskog, Cray Research, Teledyne, ATX, a Saatchi leaves Saatchi, Mesa, Hollywood's boffo holiday box office

International Business

51 INTERNATIONAL OUTLOOK

Political pandemonium could fracture Italy's economy

Economic Analysis

26 ECONOMIC VIEWPOINT

Becker: Proposition 187 is on target—now rewrite federal law, too

30 ECONOMIC TRENDS

Consumers get squeezed by rates, U.S. capital exports dwindle, big recreation bucks, another look at IRA tax breaks

31 BUSINESS OUTLOOK

Christmas, 1994: Shoppers came, bargain-hunted, and bought

Government

49 WASHINGTON OUTLOOK

Old MacDonald has a subsidy, and the GOP has a dilemma

Finance

52 INSIDE WALL STREET

A slot Redstone drops money into The drug that may keep Elan hopping Upping the pulse with this implant

129 INVESTMENT FIGURES OF THE WEEK

The Best of 1994

101 A BUMPER CROP OF KUDOS

What Apple's Michael Spindler, Merck's Judy Lewent, and the Myst CD-ROM have in common: They're among the best

Personal Business

120 COMPUTERS: Crying for help

SMART MONEY: Construction stocks **ESTATE PLANNING:** Trust funds

Features

6 UP FRONT

13 READERS REPORT

14E2 LETTER FROM FLIGHT 754

A nervous flier climbs into the cockpit

15 BOOKS

24 TECHNOLOGY & YOU

127 BUSINESS WEEK INDEX

128 INDEX TO COMPANIES

130 EDITORIALS

Up Front

EDITED BY LARRY LIGHT

WE POLISHED THE CRYSTAL BALL, AND...

IT'S OUR SECOND ANNUAL trip out onto a limb. Last year, we were right on a paltry 4 out of 10 predictions. We predicted that Arnold Schwarzenegger would make a movie comeback, for exam-

ple, but we goofed in saying the Fed would hike rates just a half-point. So, in the spirit of often wrong but never in doubt, here are 10 more for 1995:

CONTRACT WITH AMERICA. Newt Gingrich's agenda won't pass in toto during his first 100 days as House Speaker, as pledged. The Georgia Republican will get the easy ones, such as a middle-class tax cut and a hard-line crime bill. But he'll have to wait on more controversial fare: a capital-gains-tax reduction, welfare revamping, tort reform.

INTEREST RATES. The Federal Reserve will keep on tight-

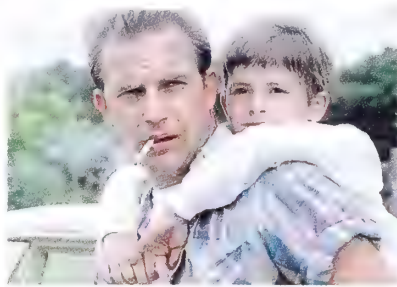
ening, but only in the first half. Look for the federal funds rate to rise about a point, to 6.5%. To avoid spooking Wall Street, Congress will balance a tax cut with spending reductions, so the Fed won't fear budget-busting. With the economy slowing around midyear and inflation under control, the Fed will then coast.

STOCK MARKET. Held back by rate increases and a ratcheted-down economy, the market will slump a bit early in the year. In late 1995, though, continued strong corporate profits and increased overseas demand will perk up Wall Street's spirits. The Dow will hit 4100.

WORLD TRADE. Passed with great flourish by Congress in 1994, the General Agreement on Tariffs & Trade will get its first test—and the results won't be pretty. A nasty squabble over who will head the World Trade Organization, which oversees GATT,

TALK SHOW "Prophecy: The art and practice of selling one's credibility for future delivery."

—Ambrose Bierce, *The Devil's Dictionary*



PERFECT WORLD: New duds ahead?

GENERAL MOTORS. The world's No. 1 carmaker, with its North American operations once again profitable, will spin off its Hughes Electronics and Electronic Data Systems.

HOLLYWOOD. Kevin Costner, at one time among a core group of marquee-value leading men, comes a cropper

with Universal's summer release, *Waterworld*. The flick is way overbudget and a conceptual mess. This comes after two Costner bombs, *The War* and *A Perfect World*.

WINES. Prices for class French wines will rise 15% to 25% in the U.S. after four level years. American consumption is climbing, and mediocre recent vintages from France mean smaller supplies of the good stuff. In November, prices paid for premium Burgundies were up 50% from a year ago.

SECURITIES REGULATION. The securities industry will succeed in its campaign to limit the information that may be released about a broker's reputation—namely, with holding pending complaints and details of past rulings that favored the brokers.

will turn member nations resentful and leery.

DEBT CRISIS. A major First World debt crunch will hit three nations facing out-of-control budgets and political

paralysis: Italy, Canada, and Sweden. The World Bank and International Monetary Fund will have to move in to restructure the debt of these industrialized countries.

MERGERS. Dr Pepper/Seven-Up will be swallowed by the British beverage giant Cadbury-Schweppes. Dr Pepper, now that it's back in the pink, is a good strategic fit for Cadbury-Schweppes, which already owns 26% of the American soft-drink outfit.



FRENCH WINE: Costlier sips



FEARLESS

SMARTEST MOVES OF 1994

1. Here's to the investors who limited their exposure to derivatives, which were pounded when rates soared. Thank heaven not everyone is as foolhardy as Orange County.
2. The Dream Team of Steven Spielberg, Jeffrey Katzenberg, and David Geffen got together. How can this trio lose? First beneficiary: ABC.



THE DREAM TEAM: *Advantage, ABC*

3. Newt Gingrich's Contract With America, whether it works out or not, was the marketing coup of the year. It nationalized the election and gave Congress to the GOP.

4. Self-appointed peace broker Jimmy Carter eased the crisis with saber-rattling North Korea and restored democracy in Haiti. May-

be even his Bosnia efforts will pay off.

5. Bill Gates put the feds' antitrust inquiry into Microsoft behind him. The result? Rivals say the software giant hasn't been reined in at all.

DUMBEST MOVES OF 1994

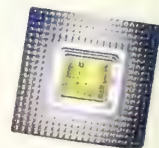


BASEBALL: *Popping out*

1. Bill Clinton bet big on passage of a government-heavy health-care reform package—and then handled things badly, severely wounding his Presidency.
2. Its Pentium chip flawed, Intel treated worried customers with arrogance. It waited six months after finding the glitch before offering replacements to any who asked.
3. Disney's plan to plunk a theme park in history-rich rural Virginia was a public-relations disaster. Mickey's Bull Run-style attack ended in a rout.

4. Baseball owners forced a strike, ending an exciting season. Greedy players went along. Result: long-term trouble.

5. Fidelity Investments promised Magellan Fund investors \$2.3 billion in distributions before realizing it had made an accounting error. Never mind.



PENTIUM: *Intel goofs*

JAN 25 '95 11:24 AM

TWIN FIRES

PAGE 001



FAX DELIVERY NOTIFICATION

INQUIRY FROM: JOHN MC GARRY
TWIN FIRES INC
710 W 34TH ST
NEW YORK NY 10011

SHIPMENT TO: JUSTINE FASCIANO
KAMIN & ASSOC INC
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CHICAGO IL 60610

Shipper number.....	149X08	Pickup Date.....	1/23/95
Number of Parcels.....	1	Shipper Invoice Number.....	1
Shipper Reference Number.....	1	Tracking ID No.....	04715934057
Pickup Record Number.....	1	Merchandise.....	LETTER

According to our records, 1 parcel was delivered on 1/24/95 at 400 E Chestnut St
The shipment was signed for by J. Fasciano as follows.

Signature

Justine Fasciano

.. TOTAL PAGE 001 ..

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EVERYONE HAVE THEIR No. 2 PENCILS?

SO YOU THINK YOU'RE REAL informed, huh? Let's test your business-news acumen with this little pop quiz.

1. Whom did General Electric install as temporary head of troubled Kidder, Peabody, pending sale of the firm to Paine Webber?

2. What did investor Kirk Kerkorian want Chrysler to do?

3. Who bought Channel 1 Entertainment, the television service for schools, from Chris Whittle?

4. How old a company is Coca-Cola?

5. What is the top-selling vehicle in the U.S.?

6. How did Prudential Insurance flout tradition?

7. Who squelched the CBS-QVC deal?

8. She's only the second woman to head a Federal Reserve regional bank. What's her name?

9. How long was Robert Citron the treasurer of Orange County, Calif.?

10. What was the first Las Vegas casino that ITT bought?

11. Treasury Secretary-appointee Robert Rubin has what common background with Bill and Hillary Clinton?

12. What was the earlier career of fallen biotech investor David Blech?

13. Which Federal Reserve official's dovish comments at its

Jackson Hole retreat caused a Wall Street uproar?

14. Who is the new chief executive officer of Merck?

15. Who bailed out Euro-Disney?

16. What was the downfall of ousted Continental Airlines Chief Executive Robert Ferguson?

17. How many times did the Federal Reserve raise interest rates in 1994?

18. What was Silvio Berlusconi's line of work before his election as Italy's prime minister?

19. Sears Roebuck Chief Executive Edward Brennan changed his mind about a major operating unit. What was Brennan's decision?

20. What is adman Carl Spielvogel's new gig?

21. Name the first Cabinet-level Clinton appointee to leave.

22. Who will be the new chairman of the House Budget Committee?

23. Whom did Michael Dell import to share CEO duties?

24. What American company did Swiss drugmaker Sandoz buy?

25. What two archrivals in the steel industry are teaming up?

26. What is the title of Sir James Goldsmith's anti-GATT book?



CITRON: It's over

TRIVIA

QUIZ



RUBIN: Boola-boola



WHITTLE: Cashed out



PILOT ERROR: CEO ejected

THIS SHOULD GLADDEN NEWT'S HEART

THE SECOND ANNUAL UP Front readers' Fax Survey shows a group that doesn't expect to collect a gold watch from its current employer, casts a baleful eye on welfare spending, and looks for the best returns in 1995 from the

FAX SURVEY

ever-volatile stock market. A bunch that puts a premium on self-reliance, you might say. Drawing 350 responses over the fax ma-



JOB SECURITY? Dream on

chine (and some from old-fashioned mail and even one via the Internet), our survey is no scientific cross-section. But it shows what's on readers' minds.

Take their jobs. In a time of rampant layoffs, almost a third feel less secure at

work than they did a year ago. And almost as many don't expect to be around a year from now—whether through management's choosing or their own. By decade's end, more than half believe they will be history.

On national matters, our respondents target welfare as the worthiest candidate for federal cuts. That's despite the fact that welfare spending makes up a minuscule 1% of government outlays. Social Security, a largely middle-class entitlement program that pays out far more, is way down on the cut list. Similarly, most consider welfare the biggest problem, far exceeding those who want to lop corporate welfare—subsidies to business.

We asked what law folks wanted to see passed, if they had the power. Over all, the answers would warm Newt Gingrich's heart, such as the line-item veto, a balanced-budget amendment, school prayer. Our fave: index congressional pay to the gross domestic product.

How do you feel about your personal job security, compared with a year ago?



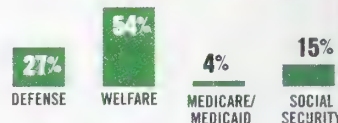
Do you expect to be working for the same company a year from now?



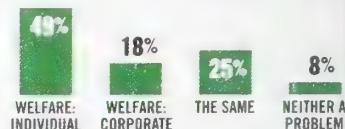
Five years from now?



To help balance the federal budget, slice which the most?



Which is a bigger problem?



What will be the highest return investment in 1995?



ANSWERS: 1) GE CEO Dennis D. Sullivan; 2) Do a stock buyback; 3) Kohlberg Kravis & Roberts; 4) 100 years; 5) Ford F-series pickup; 6) Made an outsid-er CEO; 7) Comcast, a cov. shareholder; 8) Cathy Minehan of the B...; 9) 24 years; 10) Desert Inn; 11) A Yale law degree; 12) Musician; 13) Alan Blinder; 14) Raymond Gilmartin; 15) Prince A. Walid of Saudi Arabia; 16) Problems at Continental Life; 17) Six; 18) Ripping his media conglomerate; 19) To spin off Allstate; 20) Head of a car dealer chain; 21) Defense Sec-etary Les Aspin; 22) Representative John Kasich (R-Ohio); 23) Motorola vet-Morton Topfer; 24) Gerber; 25) U.S. Steel and Nucor; 26) The Trap

In today's uncertain markets, when are "strength and stability" more than just buzzwords?

When they're backed by an impeccable balance sheet and healthy profits.

If you're concerned about the financial strength of your insurance and financial services organization, here are some questions you should ask.

What's the clearest indicator of financial health?

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Moody's **Aaa**

A.M. Best Co. **A++***

*Domestic Property-Casualty Companies

How important are the designations awarded by the rating agencies?

Very important. They provide an impartial, thoroughly researched measure of a company's financial strength. AIG holds the highest ratings awarded by the principal agencies. They are a prized asset,

enabling us to capitalize on business opportunities not open to those without these credentials.

Are there substantial differences in the way insurance organizations are managed?

Yes. Take investment and underwriting philosophies. In investing, AIG has an insignificant exposure to high-yield securities and commercial real estate,

which have caused so many problems for other companies.

The overall quality of our assets is excellent, with new cash flow invested primarily in investment-grade fixed-income securities.

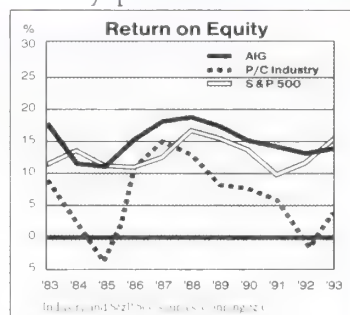
We also believe underwriting profits are fundamental to the long-term stability and health of a company.

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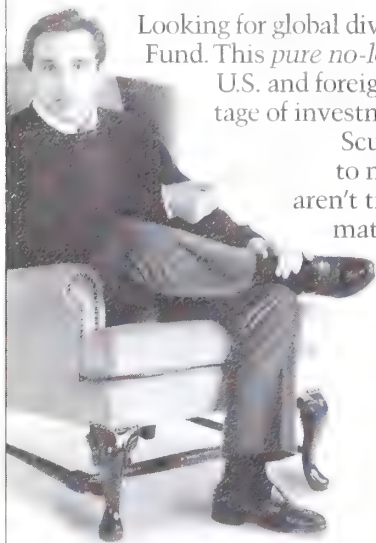
So if you're looking for financial strength, stability and commitment for the long term, as well as the other qualities AIG has demonstrated for years—creativity, service and a willingness to consider new ways of solving financial problems—we want to hear from you.



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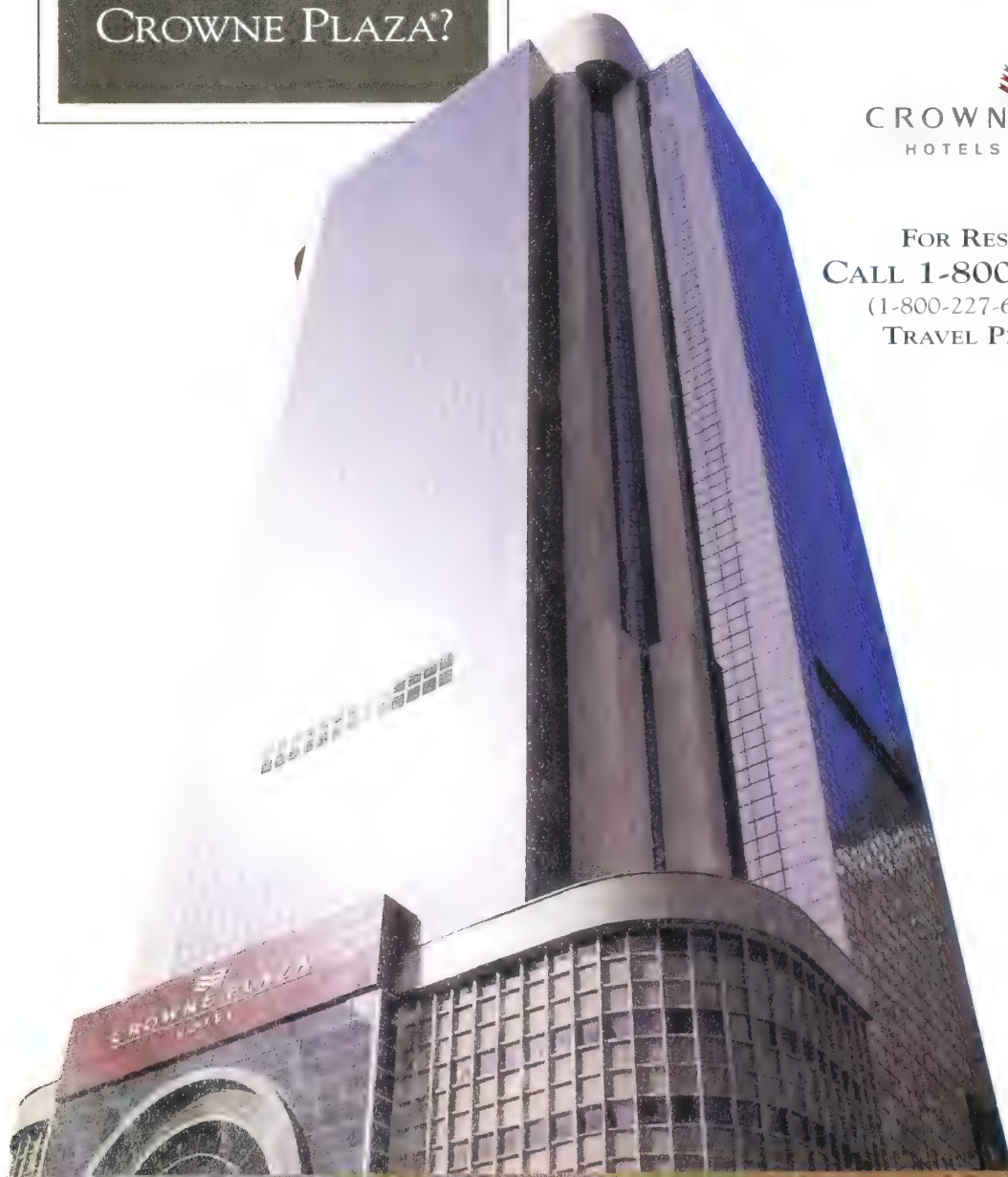
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WHERE THERE'S SMOKE, THERE'S INSIDER TRADING

In your article "Insider trading" (Cover Story, Dec. 12), it strikes me that insider trading in the stock market bears a strong resemblance to another type of cheating associated with another type of gambling: playing poker with a marked deck. After the cheat makes his money from the uninformed, he disposes of the marked deck and claims his gains were due to superior skill. By then, who can disprove him? Let's not forget that gambling produces neither products nor services. It is based on the bigger-fool theory—just like the market.

Wayne L. Stephanoff
Las Vegas

I would propose that the government make sentences for insider trading very

severe. If the punishment were a stiff prison term and heavy fines for any involvement, no matter how much money was made, then you would see many people think twice before they get involved with making a quick buck.

Diego Scaglione
Belleville, N.J.

"The company knows of no reason for the heavy trading in its stock."

Anyone releasing that comment in the midst of secret merger talks believes in the old adage: "Where there's smoke, there must be spontaneous combustion." You have two companies "secretly" locked in merger negotiations for a week or so, during which time the prospective acquiree's stock price "mysteriously" rises 60% on heavy trading. However, it appears that everyone at the negotiating table was too busy to notice the runup—or to speculate on what or who may have caused it. Right.

In just about every instance mentioned in your article, the companies could have prevented some—perhaps a large part—of the gun-jumping that appears to have occurred if they had acted

promptly in accordance with standard guidelines issued by all of the major U.S. stock exchanges and market systems:

- Restrict access to material information to the least possible number of executives and advisers.
- Monitor market activity continuously.
- "If unusual market activity should arise... make an immediate public announcement of the matter" (*NYSE Listed Company Manual*).
- Request a halt in trading until the news can be widely disseminated.

To the extent that they disregarded these clear-cut directions, the companies listed in your survey failed in their duty to promote a fair and equitable market in their securities. The oldest rule of investor communications applies here: When in doubt, disclose.

William Braznell
Larkspur, Calif.

WHEN IN DOUBT, DISCLOSE

"To the extent they disregarded the exchanges' clear-cut directions, the companies listed in your survey failed in their duty to promote a fair and equitable market in their securities."

WHAT'S SO RADICAL ABOUT A TAX CUT?

Not only do I take strong exception to Rudi Dornbusch's analysis in "You can't cut taxes and balance the budget" (Economic Viewpoint, Dec. 12), but I am sick and tired of pseudo-intellectual, ivory-tower types who use words like "radicalism" to describe Newt Gingrich and the Contract With America in an attempt to frighten people into their camp.

Is it radical to want fiscal responsibility? Is it reckless to allow people to keep more of their earnings? Is it perverted to shrink the size and scope of government? The ugly truth is that the distorted view that government can't balance its budget or that tax cuts result in deficits has resulted in the ever-increasing growth of government.

Jim Baumgardner
Hillsboro, Ore.

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Rudi Dornbusch demonstrates that economics is still an art and not a science. All tax cuts are not bad (nor are they the same), and all balanced budgets are not good. A \$500-per-child tax credit would clearly be a stimulus to the economy since it puts more money in the hands of the people who need it to spend on their family. A capital-gains tax cut that rewards long-term investment would provide the financial stability and fuel for long-term growth without cutting deeply into tax revenues.

Gerald M. Lavey
Humble, Tex.

THE NATION IS STILL PAYING FOR REAGANOMICS

Regarding your article, "Deja voodoo all over again?" (News: Analysis & Commentary, Dec. 12), I was dismayed. George Santayana was right: Those who fail to learn the lessons of history are doomed to relive them.

The country is currently \$4.6 trillion in debt, mostly as a result of the financial policies of the Reagan Administration. The interest payments on that huge amount have severely restricted the government's ability to operate. I sincerely hope that our new (and old) members of the Senate and House see through these flawed theories.

A. F. Frost
Roswell, Ga.

PCs: WHERE BIGGER ISN'T BETTER

I am only 13 years old, but I am an avid follower of computers and read your magazine every week. I find many of your articles very interesting. However, it makes me a little uneasy when I see articles emphasizing to go big, now ("Home PCs for the holidays," Technology & You, Dec. 12). I have a 486 DX2/66 microprocessor and a hard drive with 500-odd meg (and a few extras, such as a modem), the exact description of what you call "a power user's dream just a couple of years ago." Suggesting that such a machine is outdated disturbs me. I understand that the computer industry progresses, and things get outdated. But the new hardware doesn't brighten your day like new hardware used to.

Right now, I can run any IBM-compatible program at speeds that don't create inconvenience. I have multimedia and "edutainment" to my heart's content. And I can do calculations correctly (unlike some other machines I know). In my opinion, the computer market is at a point where bigger, better, faster won't be bigger, better, and faster until a bigger, more impressive advancement comes along.

Zack Michaelson
Winston-Salem, N. C.

FDA DELAYS HURT MORE THAN JUST BUSINESS

From his "Reality Check" (Up Front, Dec. 12), it is evident that John Carey has not adequately contemplated the impact of Food & Drug Administration delays on the availability of treatment advances for patients and on the prospects for the health of medical research and development.

His statement that FDA approval is desirable from a marketing perspective demonstrates a failure to understand that the principal goal of both physicians and health-care manufacturers is to improve health and avert suffering as promptly and effectively as we can. His AIDS example obscures multiple real problems.

A case in point: An FDA-instigated,

WHAT PRICE DRUG SAFETY?

"Patients in [other] countries receive benefits of new treatments much earlier than we do."

several-year delay in the approval of transvenous implantable defibrillators for preventing cardiac arrests caused by ventricular fibrillation has resulted in numerous patients being unnecessarily subjected to open-heart operations, with the inevitable risks and mortality.

Compare clinical outcomes in the U.S. with developed countries where the time for regulatory evaluation of new products is typically many years shorter. There are no current examples of diminished patient safety as a result of more efficient regulatory assessment in either Canada or Western Europe. And patients in those countries receive the benefits of new treatments much earlier than we do, even though in many cases the treatments were actually devised by U.S. physicians and corporations.

Dr. David G. Benditt
Professor of Medicine
University of Minnesota
Minneapolis

As the FDA proves new products are safe and effective, many devices with future possible diagnostic implications will never be used. Small companies, such as ourself, will not sell a new product that generates \$3,000 to \$5,000 per year if we have to pay, up front, \$10,000 to \$20,000 to get it approved by a bureaucratic FDA.

Donald A. Jorgensen
Kent Laboratories Inc.
Redmond, Wash.

Your Reality Check is typical of someone who has never needed a new treat-

ment or participated in a new drug study. If someone has advanced Alzheimer's disease, is given a drug already shown to be safe (keeping in mind that nothing can be guaranteed 100% safe) and the person shows a complete recovery within days—that's good enough for me. To approve all treatments the same way is unfair to people who need and are willing to take a chance with a new treatment in a controlled manner.

William Blaze
Walworth, N. Y.

NATIONS BANK: TO TIE OR NOT TO TIE

We are quoted in the BUSINESS WEEK article "NationsBank: An excess of zeal?" (Finance, Nov. 28), and we are disappointed. Many of the quotations are inaccurate and out of context. Additionally, comments that would significantly change the tone of the article were omitted.

Contrary to what the article attributes to us, we do not believe there was any tying or coercion on the part of NationsBank in connection with our industrial revenue bond issue or our discussions. In fact, we explicitly stated there was no tying: "No one at NationsBank ever stated that issuance of their letter of credit was contingent upon them acting as bond agent—we know there is no tying."

What appeared in print is not what we intended to say or actually believe.

Tyler N. Crafton
Senior Vice-President
Lynn F. Howard
Vice-President for Finance
Consolidated Engineering Co.
Atlanta

Editor's note: Our reporter's notes, based on two interviews, are clear on this point. They do not show Crafton and Howard denying that the incident was tying and do show them saying that they were heavily pressured by NationsBank. Based on that, and other information, we stand by our story.

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"WE TRUST NOTHING": *United's Krakowski gives Kelly a tour*

kowski, who has flown aircraft of one sort or another for 24 years, led me through a maze of busy offices a floor below the C Concourse. We proceeded to a room filled with pilots where he and Crawford pored over weather charts, examined the day's flight path, and studied a printout detailing our plane's mechanical history.

Because of the poor visibility, Krakowski immediately requested more fuel—in case we had to circle Atlanta. The only other concern was clouds above

Tennessee that might cause turbulence. Pilots, Krakowski explained, aren't bothered by snow or clouds—only thunderstorms. "Flying through one of those can cause structural failure," he intones. Translation: A thunderstorm's shifting winds, lightning, and extreme temperature changes can rip a plane apart. "We avoid them," he deadpans.

ICY WINGS. As we entered the cockpit 30 minutes before flight, Krakowski and Crawford, a former Air Force pilot who once flew U2 spy planes, began preparing for flight following a highly standardized set of procedures. There seemed to be a strict routine for everything, including eating breakfast in the cockpit. To start, the plane generators are turned on, cabin pressurization checked, collision avoidance system tested, and so on, using the same order on every mission to avoid mistakes. Nothing is left to chance: There are six checks during the flight—before pushing back from the gate, before takeoff, after takeoff, while descending, just before landing, and after arriving.

As we prepare for takeoff, a wet snow is falling, and ice is the big worry. About 20 minutes before departing, our plane is de-iced with the new Type 2 fluid, which is supposed to keep the wings ice-free longer because it isn't as water soluble. Krakowski and Crawford open the side windows—which function as the cockpit escape route in a crash—and scan the

AIRLINE SAFETY: THE VIEW FROM THE COCKPIT

It didn't take long for my nerves to act up. As I listen to the preflight briefing for United Airlines Flight 1268, Captain Hank Krakowski casually notes that a cloud ceiling has settled at 1,000 feet above Chicago's O'Hare International Airport and that it might be dropping by the time the Boeing 737-300 rolls down the runway Atlanta-bound at 6:50 a.m.—one hour away. To add to my jitters, First Officer Alan Crawford points out that conditions are worse in Atlanta: a cloud ceiling of 400 feet with fog. I gulp. Should we even attempt flying under such conditions? Is it too late to go back home and crawl into bed? "Don't worry," Krakowski assures me cheerily. "We can bring the plane in as long as we can see the runway 50 feet before landing."

Uh-huh. A 55-ton jet plane traveling more than 200 mph, carrying 128 people and more than 12,000 pounds of expensive aviation fuel? I'm finally fulfilling a long dream of sitting in the "jump seat"—the chair behind the captain and pilot—to experience what flight is like

from the vantage point of the cockpit. But now I'm not so sure. The issue on which I justify this reporting trip—airline safety—has become all too real. In September, a USAir 737—similar to the one I'm on—careened 6,000 feet into a hillside outside Pittsburgh, killing the 132 people on board. That was quickly followed by two fatal American Eagle accidents, including one just 90 miles from here in Roselawn, Ind.

A trip in the cockpit is an education in flight safety. I've been up since before dawn. When I arrived at United's flight operations center at O'Hare at 5:50, the cockpit crew was already at work. Kra-

We're making our approach—then the visual display of the runway goes blank

wings at least three times to be sure no snow has accumulated. Ice reared its ugly head again on our return flight—at 7,000 feet, during our descent. Krakowski used a system that heats the wings and engines to prevent buildup.

Despite the snow and low clouds, our takeoff goes smoothly. Once airborne, our cramped cockpit (6 feet, 6 inches high by 8 feet wide—and cold, thanks to uncarpeted steel floors) turns into a computer junkie's dream. A digital map charts our progress to Atlanta against the flight plan, and constantly checks to make sure the pilots are on course. A collision avoidance system displays the altitude of the few planes in our vicinity and can suggest evasive action should one wander too close. And a flight data system spits out information on Atlanta's worsening weather, provided by personnel back at United's Elk Grove Village, Ill., headquarters. The pilots begin to discuss the possibility of a rare autopilot landing while monitoring a steady stream of instructions from air traffic controllers along the way.

Best of all, if any of the systems should shut down, there are backups that provide the same data. This came in handy during our return from Atlanta. Banking left in cloud cover at 5,000 feet, our flight director, a visual display that shows pilots whether they are correctly lined up with the runway, temporarily went blank. Though my heart stopped, Krakowski and Crawford soldiered on, relying on two other gauges which provide the same data, just not in graphic form. I didn't find out about these displays until after we had landed.

Of course, the primary backup is the human eye. Before ascending to the cruising altitude of 35,000 feet on the return to Chicago, the pilots look out the window to confirm that a jet has passed overhead—even though the collision system registered its passing. And during our 35-minute layover in Atlanta, Krakowski and I walk around the plane, checking for cracks or ripples in the steel and for hydraulic leaks, any of which can doom the aircraft. Computers might have provided the information, but says Krakowski: "We trust nothing."

Conditions en route to Atlanta dic-

tate that we rely on technology to an extraordinary degree. As soon as we reach our 500-mph cruising speed on our 600-mile journey, we start hearing air-traffic reports about a low cloud cover at Atlanta's Hartsfield International Airport that is forcing planes to abandon landings there. And 40 minutes into

the flight we learn that Knoxville is completely fogged in, so we must switch our alternate landing site to Birmingham, Ala. That causes a flurry of calculations by the crew to determine how much fuel it would take to reach Birmingham.

Then comes the bad news: 20 minutes before our scheduled landing, we're told to circle at 24,000 feet and are warned that we may be there for up to 30 minutes. The pilots start calculating—by hand—how long they can wait and still have fuel enough to make Birmingham. Fortunately, after 10 minutes, we're cleared to start our approach.

Now my heart really begins to beat faster. Because visibility is so poor, Krakowski has decided to go ahead with the autopilot landing. "You're lucky," he says. "We hardly ever do this." How lucky do I feel? Not very. Krakowski says pilots average about one weather-related autopilot landing a year, but assures me that pilots train for them often.

WELCOME LIGHTS. Krakowski starts by plugging the landing strip coordinates into the system, even though the plane is guided by a radio signal to the end of the runway. My nervousness is piqued by the air traffic controllers who are barking orders at planes buzzing around Atlanta's crowded skies. As we descend through clouds, the cockpit grows darker. The crew lowers the landing gear and wing flaps. The engine thrust and yoke move eerily on their own, controlled by computers, though Krakowski rests his hands on the controls, prepared to take over if need be. With 600 feet to go and clouds obscuring the runway, I can only hope we're on target. Seconds later, my prayers are answered—flashing lights appear straight ahead as the clouds part.

No doubt I feel safer for this experience, no small matter for me. I've been a nervous flier for more than a decade, after a flight I was on plunged 1,000 feet in an air pocket as we descended for landing. Since then I haven't been able to sleep the eve of a flight. But knowing that the guys (and women) in front are as manic about safety as I am helps. Despite the nerve-racking headlines, the folks back in the cabin might rest easier, too, they saw what I saw in the cockpit.

KEVIN KELLY

Chicago correspondent Kelly used to cover airlines.

CAPTAIN'S LOG: CHICAGO TO ATLANTA

CHICAGO

6:40 A.M.: As we prepare for takeoff, snow begins to fall. Pilots see that plane is de-iced. They open side windows to see that the snow isn't sticking to the wings.

7:31: After holding at 20,000 feet for traffic, we are cruising at 33,000. Because Knoxville is engulfed by fog, our alternate airport is switched to Birmingham.

8:06: Weather has grown worse in Atlanta. Planes are stacking up, so we slow down and pilots start plotting when to divert, should fuel become low.

8:18: Plane is being buffeted by turbulence. ATC has told us to enter a holding pattern. Pilots have done more fuel calculations (by hand) and decide to land using the autopilot, a very rare event.

7:45: Pilots start checking fuel and talking about how much it would take to reach Birmingham should we have to divert.

8:39: Descending into the clouds for final approach. Contact the tower to confirm autopilot approach. Pilots redo fuel calculations again. Call out landing checklist. Landing gear lowered.

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ORWELL'S REVENGE
 The 1984 Palimpsest
 Peter Huber
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WHY BIG BROTHER ISN'T WATCHING YOU

Ever since George Orwell's *1984* appeared in 1949, there has been no forgetting its searing vision of vicious, totalitarian state that uses technology to maintain a vise-grip on citizens' thoughts. The infamous year is now but a decade past, American democracy intact, and Soviet-style communism all but gone. But *1984*, like Orwell's name, retains its power as an emblem of technological intrusion. It's fascinating to wonder what Orwell's Big Brother might accomplish with today's expanding array of computer networks, Infohighways, "smart cards," satellites, artificial intelligence, and miniaturized video cameras. Actually, very little, argues Peter W. Huber in this intriguing and stylish new book, *Orwell's Revenge: The 1984 Palimpsest*. We have nothing to fear from technology, says Huber—at least not so long as free-market forces, rather than government, determine how the technologies get used. A senior fellow at the Manhattan Institute for Policy Research, a conservative think tank, Huber seeks to discredit not only *1984* but also Orwell as a thinker and every aspect of the social vision in which he believed.

Huber begins by reminding us how heavily *1984*'s Party members depend on the "telescreen" to maintain their hold on the populace, then points out how technically flawed that idea is. Orwell's telescreen is a TV-like box installed in every room in Airstrip One (and postwar Britain) that the Party uses both to beam propaganda to the masses and to keep an eye out for any signs of subversion. In fact, television

was just becoming popular when Orwell wrote his dark satire, and many fellow Britons misunderstood the new gizmo as being able to observe their most intimate moments. While acknowledging Orwell's writing genius, Huber argues that such a surveillance network would be impossible to maintain and operate—especially in the world of *1984*, where the masses are

kept ignorant and besotted with Victory Gin. The network would require not only qualified technicians but also countless sober citizens to monitor their fellows.

And if the telescreens don't work, says Huber, then the rest of Orwell's vision falls apart, too. Orwell conceived of his telescreen network as being under the Party's sole control—much the way the British Broadcasting Corp., where he had recently worked, served as the wartime mouthpiece for the British government. But today's Internet, a global electronic-mail network, and the 500-channel Info Highway envisioned for the future show that deregulated communications markets actually enhance democracy by allowing an unlimited multitude of ideas to circulate, says Huber. If people don't like what they see on TV, they can change channels. On the Internet, they can even create their own "channel," or discussion group, to serve any community that shares an interest. And things will only get better, Huber writes, if new communications and computing technologies dissolve the remnants of IBM's and AT&T's old monopolies.

Huber goes about his flaying of Orwell in a rather ingenious and fitting

way. To create his palimpsest (a "writing material used one or more times after earlier writing has been erased"), he first scanned Orwell's novels, essays, letters, and even wartime radio transcripts into a PC—with *1984* consuming exactly 590,463 bytes of memory. This let him quickly search Orwell's oeuvre for early expressions of ideas, descriptions of particular scenes, even figures of speech that later show up in *1984* and elsewhere—connections he uses to expand his critique to the whole of Orwell's thinking.

Then, Huber composes his own book as a clever, contrapuntal mix of fiction and essay. His computer searches turned up many instances where Orwell's thinking contradicted what he eventually propounded in *1984*. Using these passages and other colorful bits of Orwell's writing, Huber constructs a sequel involving a character called Eric Blair (Orwell's given name) and O'Brien, *1984*'s torturer-antagonist. He has O'Brien discover Orwell's wrong-headed thinking and find, for instance, that some phone phreaks have quietly liberated the telescreen network. Alternating with episodes of this story is Huber's computer-aided analysis of Orwell's thought, served up as a lucid but extremely critical essay backed by 79 pages of notes and citations.

Is *1984* hereby relegated to the memory hole, its vision and author thoroughly discredited? Hardly, for as clever as Huber is, he focuses his attack quite narrowly. Indeed, he has used Orwell simply as a foil against which to rhapsodize over free-market capitalism as it applies to the telecommunications business. Huber is well known in that industry for *The Geodesic Network*, a lengthy white paper advocating total deregulation of the national network and all its services, which has shaped policy debate since it was published in 1987.

Clearly, as Huber insists, there are more choices than ever on our telescreens, whether we call them TVs or PCs. On the other hand, even as the ethers fill with information, there's reason to question whether a free market in telecommunications will bring liberating benefits to the masses. Most discussions of the Info Highway now center on using it as an ultra-efficient sales and marketing channel—useless, it



HUBER SAYS THAT HIGH TECH, FAR FROM BEING AN ORWELLIAN THREAT, ACTUALLY SPURS DEMOCRACY

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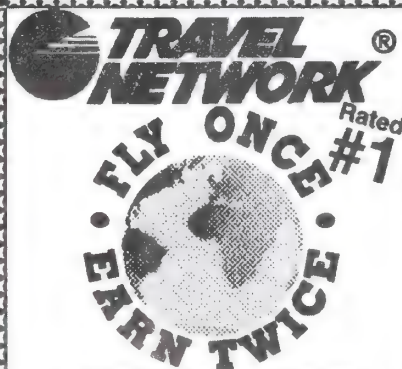


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Books

would seem, to those who can't afford connection or lack the skills to make use of it. In the meantime, Orwell's book remains as artful, disturbing, and demanding of our attention as ever.

BY JOHN W. VERITY

Verity is Information Management editor.

BOOK BRIEF

MONSTER TRUCKS AND HAIR-IN-A-CAN

By Bill Geist

Putnam • 223pp • \$21.95

LAND OF THE LOWBROW

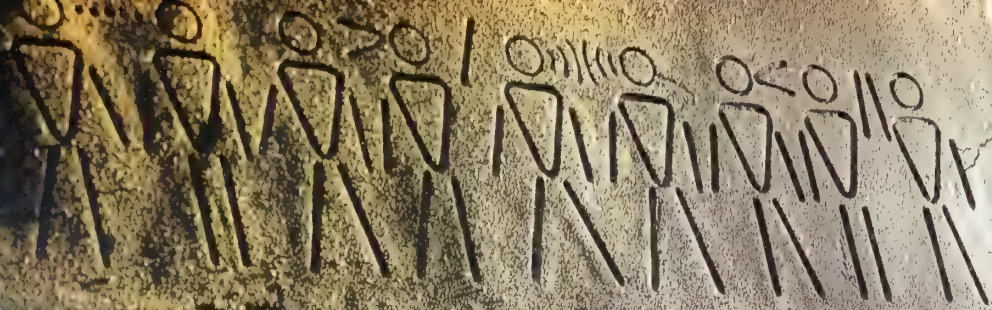
Mary Hart, a self-described "broadcast journalist," co-anchors one of America's most-watched TV shows, *Entertainment Tonight*. The secret of her—and *ET*'s—success? Her legs! For years legions of male viewers have tuned in to gawk at them, and she obliges with the Mary Hart Leg Cross—left over right toe pointed. "Are they teaching that at the Columbia Journalism School?" wonders Bill Geist in *Monster Trucks and Hair-in-a-Can: Who Says America Doesn't Make Anything Anymore?*

These days, who knows? After all, writes Geist, this is the Age of Amusement, defined "by peoples' need ... to be constantly entertained." The book is an amusing voyage through the largely fringe vocations born during this epoch. We meet the musclemen who do battle on *American Gladiators*, the cable-TV kingpin who operates the Fish Channel and the mechanic who builds the monster trucks that crush autos for sport—a "sport" that draws 15 to 20 million American spectators annually.

Perhaps the best-wrought portrait is that of Jim Reid, "the used golf ball king of Florida," who forsook a \$250-a-week job at Disney World to dive into lakes, retrieve golf balls, and sell them. By the time Geist meets Reid, his company is grossing \$1 million, and Reid is relaxing on his yacht while his minions keep diving to satisfy America's craving for cheap golf balls.

Geist, a *CBS Sunday Morning* correspondent, delivers enough chuckles to keep the pages turning. However, the quality of these pieces varies widely and a few of them stretch on far too long. Still, if you ever daydream about changing jobs, read *Monster Trucks*. There are more possibilities than you ever imagined.

BY KEVIN KELL



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EDITED BY STEPHEN H. WILDSTROM

CD-ROMs: A MUST FOR THE OFFICE?

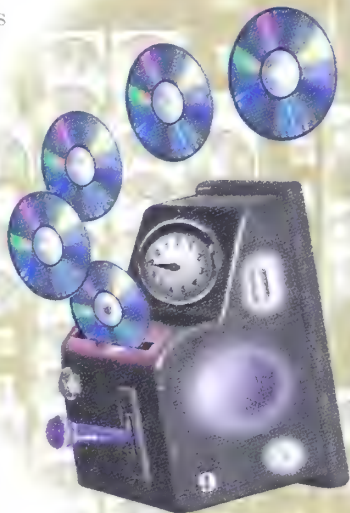
What's round, noisy, and should probably be found in more offices?

A CD-ROM. Drives that read these high-capacity disks have become standard equipment on personal computers sold for home use, and one major mail-order vendor, Gateway 2000, includes a CD-ROM drive on all desktop units. But the drives are still rare in the office. Perhaps that's because CD-ROMs first won wide use for multimedia games. I'm not suggesting that you spend your working hours playing *Myst*. But I do think it's time you considered putting a CD player—and audio capability—on your desktop.

The most obvious reason for adding a CD-ROM, or making sure your next computer comes with one, is that it's the easiest way to install software. Popping one CD into the drive is a lot less trouble than putting in one floppy disk, then another, a dozen or more times to load a typical office-software program onto your hard disk. Cheap and easy availability of a wealth of reference materials and effective new multimedia computer-training materials also earn CD-ROMs a place in the office.

POKEY PARADOX. More and more software is turning up in the CD format. And programs shipped on CD-ROM generally offer some sort of bonus. For example, the CD version of Borland International Inc.'s Paradox database includes an extensive

set of videos that use narration and on-screen animation of the program to teach you how to use the software. The disk also illustrates multimedia limitations: It includes an on-screen version of the Paradox documentation that is hard to read and painfully slow to use—even on a fast



Pentium-equipped machine.

Software on CD-ROM is a convenience, but reference materials offer something special. Finding street addresses and Zip Codes in a distant city can be a tedious chore. *SelectPhone* from Pro CD Inc. (508 750-0055) crams the contents of every U.S. phone book's white pages, and then some, onto five CDs for \$160. A speedy search program (like many other CD-ROMs, *SelectPhone* works on both Windows machines and Macs) allows you to search the database using an assort-

ment of variables, including name, street address, Zip Code, or phone number. A separate volume covers Canada, and if you need regular updates, subscriptions are available.

Other offerings cover a vast range. Microsoft Bookshelf, at \$65 for a Mac or for an IBM-compatible PC, provides a full set of desktop reference materials, including dictionary, thesaurus, and almanac. At the other extreme of specialization, government agencies offer data ranging from detailed census information to the federal budget. Prices vary widely. Contact your nearest Government Printing Office bookstore for prices and availability.

SOUND ADVICE. Training may be the most innovative use of the new medium. Educational CD-ROMs from Allegro New Media Inc. (800 424-1992) for Windows word processing (Microsoft Word and WordPerfect) or spreadsheets (Excel and Lotus 1-2-3) show what can be done. These disks, at around \$40 each, let you watch and listen to an animated lesson. (Earphones can keep the noise under control so your co-workers don't start circulating petitions in protest.)

Then, with just the click of a button, load a file into your word processor or spreadsheet to practice what you've just been watching.

You can add a CD-ROM player and sound card, which you will need for Windows multimedia applications, for as little as \$200. Unless you're really comfortable with the innards of a PC, get a drive-sound card package to avoid compatibility problems. As usual, Macs are a bit more expensive and a lot easier. But whatever you own, it's time to realize that CD-ROMs and multimedia are not just for kids anymore. S.W.

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SOFTWARE

INTERNET ASSISTANT: A GIFT

Free software from Microsoft Corp.? It's true. The Redmond (Wash.) giant is offering the Internet Assistant for Word at no charge. The program converts documents created with Word for Windows into the Hypertext Markup Language (HTML) that's used on the Internet's World Wide Web. Internet Assistant can also let you browse through the Web. Microsoft says copies will be available for downloading, probably by mid-January, from its Web server.

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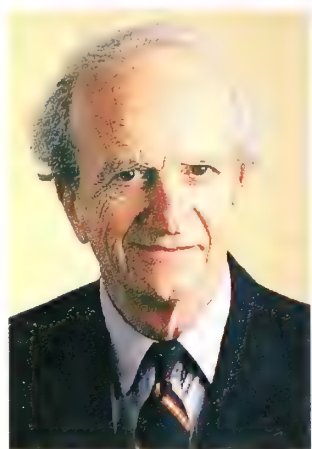
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BY GARY S. BECKER

PROP 187 IS FINE —NOW REWRITE FEDERAL LAW, TOO



VIEWPOINT:
Immigration
rules should
encourage
high-skilled
applicants.
How about
auctioning off
some slots to
the highest
bidders?

There was bitter controversy during the recent midterm elections over the state referendum in California on Proposition 187, which would disqualify illegal aliens from education and health benefits. The case for greatly reducing the number of illegal entrants is overwhelming, but the criteria used in determining who can enter legally need changing.

Stiff quotas on the number of legal immigrants were put into place during the 1920s. But the number of illegal aliens did not grow rapidly until the past couple of decades, when travel became cheaper and the desire to immigrate exploded, partly because of the benefits provided by the welfare state. Still, remarkably little is being done to discourage illegal entry.

FEW TEETH. Anyone caught is flown or bussed back to where he or she came from, most often Mexico. Many of these simply turn around and enter the country again—some have been caught more than a dozen times. Such token punishment encourages aliens to enter illegally, since it usually takes years to receive a legal permit.

The 1986 Immigration Control & Reform Act attempted to put some teeth into the distinction between legal and illegal entrants by requiring companies to check whether a job applicant had the right to be in the country. Any employer who knowingly hires illegal aliens is subject to sizable fines or jail terms. But an apparently thriving market in bogus immigration documents has undermined these sanctions.

To address this point, the drafters of Prop 187 added lengthy jail terms or fines to the California penal code for persons convicted of either using or selling false documents concerning resident-alien status to obtain a job or for any other purpose.

Most of the controversy over Proposition 187 continues to center on other sections that deny illegal immigrants access to publicly funded schooling and nonemergency health care—illegal aliens would still receive emergency care—and require school and health officials to check whether patients and students have the right to be in the country. These sections make good sense to me. Why is it more objectionable to require of school officials and health-care administrators what already is demanded of employers? And why should individuals who are ineligible for these bene-

fits because they live in another country gain eligibility by entering the U.S. illegally?

Proposition 187 received more than 60% of the vote in California, despite the opposition of most of the major newspapers in the state. Some opponents consider it a smoke screen for efforts to cut back on Mexican immigration. On a recent trip to Mexico, I was asked about this law more than about the North American Free Trade Agreement or other issues concerning relations with the U.S. To help allay fears of a cutback and possibly reduce the incentives to enter this country illegally, the U.S. could give special priority to Mexican applicants at the same time that it forcefully restricts illegal entry from other nations.

But the overwhelming case for tougher policies toward illegal aliens doesn't justify calling for a cutback on all immigration. Newcomers have added enormously to the culture and vitality of the U.S. and many other nations in the Western hemisphere. And immigration can hardly be seen as posing a threat to American culture when the foreign-born are a much smaller fraction of the population than they were 50 or 100 years ago.

TOO MODEST. However, the criteria for entry should be changed to favor those who would contribute most to the economy and would not require subsidies from taxpayers. One way to do this is to assign greater priority to young, skilled immigrants—the 1990 Immigration Act's steps in this direction are much too modest. Younger skilled workers also are less likely to become a burden by being unemployed, going on welfare, getting sick, or receiving old age support.

A radical change in admission policies now being pushed by some House Republicans would introduce a waiting period of several years before any immigrant is eligible for Medicaid, welfare, or other government program. But if radical departures from current policy are feasible, a better approach would be to follow a suggestion I made in this space long ago (BW—Mar. 2, 1987): to auction off many immigration slots to the highest bidders. Such a policy would automatically give priority to skilled applicants, since they would tend to bid the most for the right to immigrate.

The U.S. will benefit from even larger numbers of immigrants if illegal entry is curtailed and if young, skilled applicants either directly or indirectly receive top priority.

Gary S. Becker, the 1992 Nobel laureate, teaches at the University of Chicago and is a Fellow of the Hoover Institution

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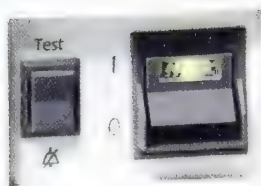
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BY KAREN PENNAR

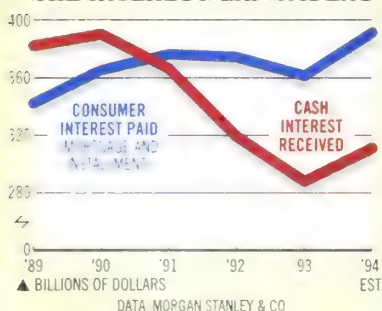
SQUEEZED BY HIGHER INTEREST

Individuals' losses outweigh gains

As rates marched steadily upward this year, consumers watched their mortgage and installment-loan costs rise. In part, these increased payments are being offset by higher returns on savings and other financial assets. Analysts at Goldman, Sachs & Co., for instance, observe that personal interest income has risen 1% or more in every month since March. And that, say the Goldman economists, will dilute the negative impact of rising rates on consumer spending.

But interest income is not the cushion for spending that it appears to be, says Stephen S. Roach, economist at Morgan Stanley & Co. Roach argues that more than 50% of interest income is derived from "imputations" by government statisticians. These are estimates of the implicit return on long-term investments such as pensions and insurance policies. Such imputed income isn't, of course, money that's available to pay off consumers' bills.

THE INTEREST GAP WIDENS



Thus, says Roach, any increase in imputed interest income can, at best, give consumers "a warm and fuzzy feeling," akin to the wealth effect derived from, say, watching the value of your stock portfolio rise.

In dollars and cents, it's more meaningful to look at what consumers must shell out in interest costs and compare that with actual cash interest received. Roach figures cash interest by deducting the portion of interest income that the government imputes from total interest income. This comparison shows that interest income hasn't covered interest costs since 1991. For 1994,

Roach estimates, interest paid will exceed cash interest received by about \$80 billion. Roach concludes that the bite from higher rates will soon slow spending.

A WORLD OF TIGHTER MONEY?

Exports of U.S. capital may dry up

Rising U.S. interest rates are likely to reverberate far away—in emerging markets. Many countries in Asia and Latin America have been beneficiaries of large capital flows from the U.S. in the past couple of years, as investors sought higher returns than they could obtain at home. Indeed, in 1993 the U.S. was the biggest net capital exporter in the world, despite its own national savings deficiency and need for capital. It functioned largely as a global intermediary for funds, shipping billions of dollars overseas, even as billions of yen were flowing into U.S. investments.

But this year's rising interest rates have already slowed America's capital exports markedly. Now, says economist William Sterling of Merrill Lynch & Co., countries that have relied on capital imports to finance domestic savings shortfalls are especially vulnerable. Mexico, for instance, was forced into a dramatic Christmastime devaluation, cutting the peso loose from its moorings to the dollar and letting it depreciate. Sterling says Colombia, Indonesia, and the Philippines may also feel the pinch of higher U.S. rates.

If the flow of foreign capital to emerging nations slows down, others may have to follow the route Mexico has taken and let their currencies float downward against the dollar. Additional measures may include raising domestic interest rates and cutting government spending.

CONSUMERS KICK UP THEIR HEELS

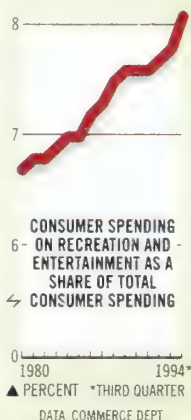
They're spending big on recreation

America has turned in a spectacular growth performance in 1994, in part because consumers have continued their free-spending ways. Fueling this boom have been purchases of consumer electronics, sporting gear, and other leisure goods and services.

Since the first quarter of 1994, spend-

ing on entertainment and recreation has risen at an annual rate of 10.5%, according to the Commerce Dept. That's almost twice the 5.5% growth rate for

THE ENTERTAINMENT ECONOMY GROWS



overall consumer spending is going much faster than the 6.9% growth in health-care outlays. As a result, the share of the consumer dollar going for fun jumped sharply to 8.1% in the third quarter of 1994 (chart).

Indeed, recreation and entertainment accounted for a full 40% of the growth of consumer spending adjusted for inflation, over the past six months. The likely reasons? With strong job growth, people have more to spend on luxuries. At the same time, the slower growth in health-care costs is freeing up money for more pleasant items.

By Michael J. Man...

IRAS: NO SPUR TO NET SAVINGS

A tax break may not be justified

Both President Clinton and Republican lawmakers have signaled that they intend to restore the tax deductibility of individual retirement accounts, the tax-deferred savings vehicles that were popular for a few years in the early 1980s, before their use was sharply curtailed. Because of their tax-deferred status, IRAs clearly cost the U.S. Treasury money. But it was never obvious that IRAs had the intended effect of increasing net savings.

Many economists and bankers suspected that people were simply shifting savings from other accounts into IRAs. Now, a new study, by economists Orazio P. Attanasio of Italy's University of Bologna and Thomas C. DeLeire of Stanford University, confirms the suspicion: Most of the money flowing into IRAs comes from existing savings. Using data for 1982 to 1986, the economists found that less than 20% of contributions represented additional national savings. This paltry share casts doubt on the wisdom of opening up an enormous tax loophole.

JAMES C. COOPER & KATHLEEN MADIGAN

THEY CAME, THEY BARGAIN-HUNTED, THEY BOUGHT

U.S. ECONOMY

To hear some of the retailers tell it, consumers didn't deck the halls with as much green in December as store owners would have liked. But if you want to know how much length consumers brought to the fourth quarter, you had better ask the shoppers themselves. As the data show, we'll get a story different from the retailers' humbug. Through November, households were flush with income, reflecting strong job growth in the second half of '94. Add in prospects of a tax cut, and it should come as no surprise that consumer confidence in December rose to a 10-year high (chart) or that shoppers used their credit cards with abandon during December.

HOUSEHOLDS: UPBEAT ABOUT THE PRESENT



...nt houses or in catalogs, which are not included in the survey.

The popularity of electronics and home products was evident in the latest *Johnson Redbook Report*. The survey reported that for all of December, sales at department and chain stores, including discounters, were up 3.3% from November and 10% from a year ago. The excellent wing for the month, which included one extra shopping day compared to 1993, reflected a strong final week of sales. Buying in the previous three weeks suggested only a cluster holiday activity.

DESPITE the mixed reports from retailers, consumer spending appears to have been strong enough to lift economic growth last quarter at a rate similar to the third quarter's sturdy 4% pace. And judging by the uptrend in factory orders through November, manufacturers will carry plenty of impetus with them into the new year, especially with the lift from improving foreign demand. Consumer outlays through November clearly showed strong momentum. Adjusted for inflation, real spending on goods and services rose a healthy 0.5% in November, after an even stouter 0.6% gain in October. Even if De-

cember buying remains unchanged from November, consumer spending is on track to rise at an annual rate of nearly 5% for the quarter.

Durable goods have been topping most shopping lists. In November, consumers pumped up their spending on autos, furniture, appliances, and other big-ticket items. In fact, from July to November, sales of furniture and appliances rose at an annual rate of 28%, the strongest four-month pace in the 36-year history of the data.

Why the buying fervor? One reason is last year's home buying frenzy. It usually takes at least 12 months before new-home buyers can afford to purchase some furnishings.

The key to the latest shopping splurge, however, is that consumers have some cash to spend. Income growth in the fourth quarter is turning out to be exceptionally robust. Although personal income dipped 0.1% in November, it had surged by 1.4% the month before after healthy increases in the two preceding months.

Adjusted for inflation and taxes, real disposable income is on a pace to rise at the best annual rate in two years. Even if December earnings do not rise, fourth-quarter income increased at a rate of more than 6% (chart).

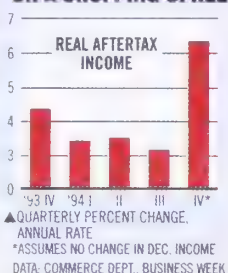
It's little wonder, then, that consumers are in such high spirits. The Conference Board's index of consumer confidence rose nearly two points in December, to 102.2, after an 11-point surge in November. It's the highest reading since June, 1990.

Households are increasingly upbeat about their present situations. That component of the overall index has jumped nearly 20 points since October. The Board attributes that spurt to falling unemployment. In particular, the number of households who say jobs are "plentiful" is rising, while those who say jobs are "hard to get" have fallen sharply.

THOSE ATTITUDES show up in spades in consumers' willingness to buy on credit. From Thanksgiving through Christmas Eve, MasterCard International Inc. reports that sales authorizations for its card jumped 35.2% from the same period in 1993. Visa Holiday Spendtrak reported a 25.6% increase in purchases made with Visa cards.

MasterCard also said card use at discount stores soared 63% from a year ago, while Visa reported a 39% increase

WHY CONSUMERS ARE ON A SHOPPING SPREE



in discount activity, larger than any other retail category.

Of course, that's good news for inflation, as price continues to be foremost in the mind of consumers, but it's not so good for the bottom lines of traditional department stores. Many retailers had to mark down prices in order to reach sales goals, and that will cut into store profits.

The only potential downer about plastic-driven holiday sales is that household spending in the first quarter may suffer if heavy credit-card bills force shoppers to take a break. Many economists have already built that scenario into their forecasts for 1995. Despite the good growth in incomes, the saving rate remains historically low, as spending rises apace with income. And those holding adjustable-rate mortgages will continue to see their monthly payments readjusted upward.

ONE SECTOR that's not likely to suffer at all in coming months is manufacturing, especially durable goods. Consumers' recent binge on big-ticket items, in addition to the ongoing boom in equipment spending by businesses, is keeping order books fat and production lines rolling.

Factory orders for durable goods rose a strong 3.4% in November, and bookings for both October and November stand well above their third-quarter average (chart). In fact, they're on track to grow more in the fourth quarter than they did in each of the two preceding quarters.

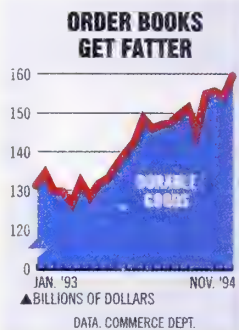
It's not just domestic demand that is keeping plants

busy. Exports are shipping at an increasingly rapid rate now that Europe is well on its way to recovery. That strength will pick up some of the slack when U.S. demand starts to wane in 1995. Although U.S. exports of goods and services dipped 0.6% in October, to \$59.7 billion, foreign shipments during the past three months are up nearly 12% from the same period a year ago.

The snag for the trade deficit is that U.S. demand—especially by consumers—still brings in gobs of imports. They rose 0.6% in October, to \$69.8 billion, as the trade gap widened to \$10.1 billion from \$9.4 billion in September.

That import wave could taper off in coming months, since retailers ordered heavily from abroad this year. Since import-dominated goods such as clothing were the very items that didn't sell well this holiday season, many stores are unlikely to reorder from foreign suppliers anytime soon.

Excess inventory also means that merchants will have to move those passed-over items at deep discounts in January. To be sure, cash registers ringing up marked-down prices will not sound sweet to retailers, but hearing the clerk say "50% off" will be music to consumers' ears.



ASIA

JAPANESE SHOPPERS AREN'T MIRACLE WORKERS

Consumers in Japan got off to a shaky start in the fourth quarter, and the uneven reports on *oseibo*—gifts given at yearend—raise concerns about shoppers' ability to rev up Japan's recovery.

Inflation-adjusted household spending fell 0.4% in the year ended in October, led by a steep 6.1% drop in households that do not rely on wage income—mostly the self-employed and elderly.

The news from wage earners was a bit better: Their spending rose for the third straight month, increasing 2.6% from a year ago. That was the largest advance in more than two years. Early reports on *oseibo*, however, indicate that consumers

pared down their gift-buying. That suggests household spending weakened as 1994 drew to a close.

Puny income gains and job jitters are prompting consumers to keep their wallets shut. Some yearend bonuses were below those handed out in 1993, and real wages and salaries in October were up just 0.6% from a year ago.

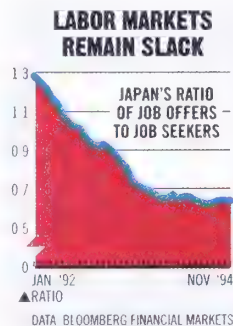
Moreover, the labor markets remain slack. In November, Japan's unemployment rate dipped, from 3% to 2.9%. That's high by

Japanese standards, especially because it misses the vast number of underemployed. And the ratio of job offers to job seekers stayed at a low 0.64 in November (chart). Also,

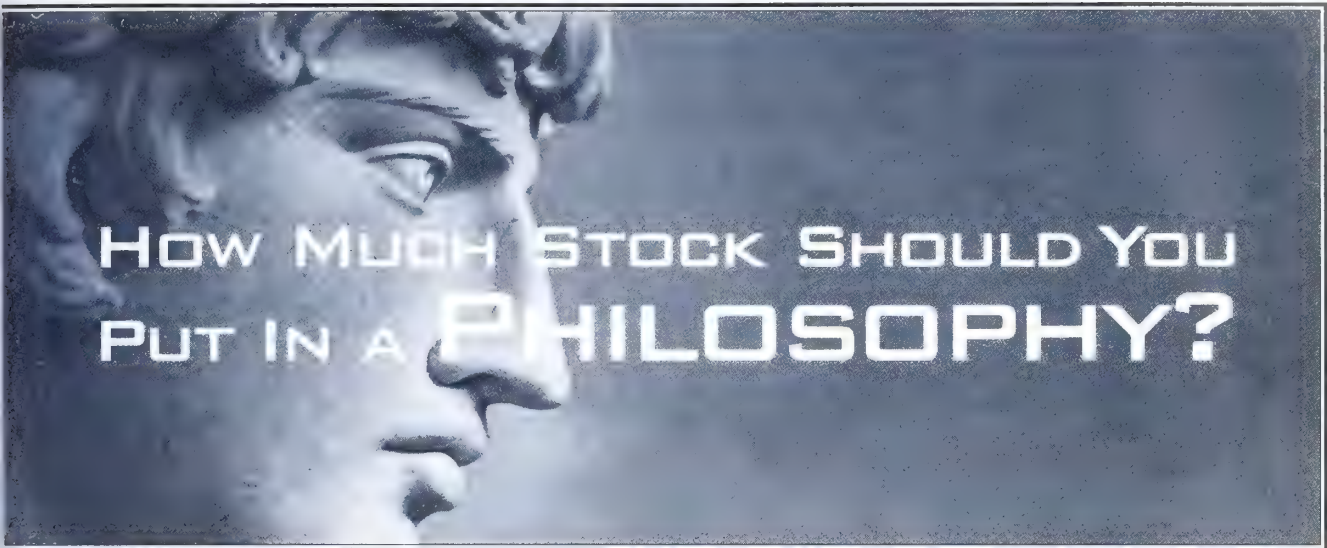
Japan's leading index fell to 50 in October, down from 58.3 in September. The latest number is at the point between readings of economic growth and weakness.

With consumer fundamentals still soft, it's not surprising that the government has lowered its economic forecast for the fiscal year ending in March. Real gross domestic product increased in the first three periods of 1994, with a gain of 3.7% at an annual rate in the third quarter.

Now, though, Tokyo says real GDP will grow by just 1.7% in the fiscal year, down from its initial forecast of 2.4%. And with Japan's economy increasingly powered by consumers—rather than exports or businesses—the reluctance of shoppers to spend may limit the vigor of Japan's upturn for most of 1995.



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MEXICO

MELTDOWN IN MEXICO

Zedillo and his team bungled the crisis. Can they revive confidence?

Over the past few months, through a presidential election campaign and an inaugural ceremony, a debate raged in the upper reaches of Mexico's government. Faced with mounting trade deficits, never-ending political tensions, and increasing concerns among international investors, should Mexico

bite the bullet and sharply devalue the peso? Despite arguments that financial markets would shake off the effects of a carefully constructed devaluation, both the outgoing President, Carlos Salinas de Gortari, and his successor, Ernesto Zedillo Ponce de León, steadfastly refused to countenance such a move.

Then, less than three weeks into his term, Zedillo did an abrupt about-face when a new flare-up of political tension in the southern state of Chiapas put even more pressure on the currency. Only days after Finance Minister Jaime Serra Puche had told global money managers that nothing of the sort was planned, the new government tried to devalue the peso by 15%—and then, with hard-currency re-

serves running low, let it fall by more than twice that (chart).

For a country that had staked its reputation on sound economic management, a strong currency to combat inflation, and heavy inflows of foreign cash to sustain growth, the comedown is humbling. Admits one Zedillo aide: "No one realized to what extent the economy was being held together with pins."

"100% ERROR-FREE." The strains hardly over. Faced with widening investor dismay and competition from high U.S. interest rates, Zedillo will now have to mount a crash campaign to keep the currency-market mess from fueling massive inflation, sandbagging the economy, and perhaps dealing a blow to the hard-won North American Free Trade Agreement. Already, corporate Mexico is shuddering at the thought of coming up with more pesos to pay interest on its \$30 billion in foreign-currency debt. Short-term rates have shot past 30%. And economists are sharply scaling back estimates for Mexican gross domestic product in 1995.

Zedillo is expected to announce his economic plans by Jan. 2. They may include short-term stabilization aid orchestrated by the Clinton Administration and the Federal Reserve, as well as longer-term measures to keep Mexico on the reformist path Salinas had blazed. Mexico needs some \$14 billion over the next



MEXICANS' PURCHASING POWER HAS BEEN SHARPLY ERODED BY THE PESO'S PLUNGE

months to cover maturing government and bank debt denominated in foreign currency, plus \$10 billion more to fund its current-account deficit, estimates rating Securities Ltd. analyst Damian Asner. And, admits one Mexican government official, "unless we come up with a program that's 100% credible and 100% error-free, we'll be facing a debacle." Even if the program is error-free, international fund managers, feeling betrayed by the Zedillo administration's clumsy handling of the currency collapse, may provide Mexico with only modest sums. They're also calling for the resignation of Serra, who alienated many with his prickly demeanor through the crisis. However attractive they make themselves, money just won't be available," says Mark Turner, Boston-based international bond guru for Putnam Investment Management. "The pigot has been tied off."

CHARACTER QUESTION. Sources in Mexico City indicate Zedillo's new reform plan will boost the pace of privatization and probably propose the sale of the state electrical utility CFE. It also is expected to include as much as a 10% cut in government spending and cancellation of budget increases that had been planned for education and other key social programs. Mexicans may also be told that curbs on salaries must continue.

Whatever reforms Zedillo attempts will

require deft maneuvering. Salinas was sometimes criticized at home for being too solicitous of foreign investors. But the wooing was necessary to convince the world that Mexico was a dependable place to invest. Zedillo, an economist, is trying to prove to critics that he possesses political skills by splitting his time more evenly between foreign and domestic listeners.

Still, the market fiasco raises questions about the character of Zedillo and his financial team. Salinas and his advisers viewed their \$17 billion trade deficit as a necessary inconvenience to modernize the country. Since domestic savings were insufficient for the huge investments companies are making to modernize, Mexico needed foreign savings.

The reasoning worked for most of Salinas' six-year term, but with one catch. Mexico proved more successful at attracting portfolio investment from mutual and pension funds than at garnering direct investment in factories. By the time the crisis broke, Americans and other foreigners held \$50 billion worth of Mexican shares, some 26% of the total market.

But as political turmoil increased in 1994, investors became more and more picky. The August elections seemed to show that Mexico had turned the corner. The September murder of a leading politician spooked the markets again. Despite



To restore faith in the peso, President Zedillo may slash spending and keep interest rates high in hopes of maintaining discipline in the markets

SOME TOUGH DAYS FOR THE PESO...



...CAP A ROUGH YEAR FOR THE MARKET



DATA: BLOOMBERG FINANCIAL MARKETS

last fall, when currency worries broke out anew. But he didn't want to be the third President in a row to leave office amid a currency collapse. And, some say, he didn't want to see higher interest rates imperil Mexico's growth.

COOLING TENSIONS. Zedillo faces a hard battle at home and abroad to restore the credibility of his month-old presidency. But Mexico, even in crisis, is still in fundamentally better shape than it was during the troubled 1980s. Its government budget runs only a modest deficit, and inflation has dropped from 160% in 1987 to 7% now. The cheaper peso also should improve Mexico's global competitiveness and give a major boost to exports. And tensions in Chiapas appear to be cooling.

In putting his 1995 plan together, though, Zedillo must mind one simple lesson: If your country wants a strong currency, you have very little room to make mistakes. At a time of huge international financial flows and mounting competition for capital, even one step off the straight and narrow may do you in.

By Elisabeth Malkin in Mexico City and Geri Smith, Joan Warner, and William Glasgall in New York

Three years ago, Michael R. Milken was sitting in a California prison camp. He had lost his career, more than a billion dollars in fines, and his freedom, but his Wall Street antennae and sense of irony were intact. As he watched investors pour billions into biotechnology almost indiscriminately, Milken recalls quipping to a friend: "If you can't find a Nobel laureate, just find somebody majoring in chemistry and you'll be able to get a couple hundred million dollars."

Today, however, some of those same companies seem like great investments to Milken. On the day he finished serving his prison sentence in 1993, Milken was handed a death sentence: a diagnosis of metastasized prostate cancer. He vowed to beat it, and, through radiation and medication, he is in remission and symptom-free. But the odds say he may have just a few years to live, and he is not content just hoping and praying for a break. He's determined to find a cure.

Milken, 48, is not the first wealthy cancer patient to become an overnight patron of research. But it's likely that the scale of his efforts of the past 22 months is unprecedented. Through CapCure, a prostate-cancer foundation he started, the former Drexel Burnham Lambert Inc. financier has written checks to 70 different scientists, sponsored scientific meetings, and is trying to organize a wide variety of resources for researchers, from videoconferencing to tissue banks. In September, Milken started his own biotech company, Cancer BioScience Corp., in Lexington, Mass., focused on prostate-cancer treatments. And now, he says, he wants to turbocharge a wider array of cancer research in the private sector.

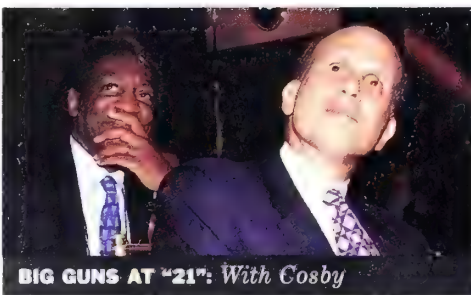
That has led him to biotech. Milken says he will soon begin investing a "significant" sum from his personal fortune in the industry and encourage other investors and large drug and chemical companies to join him. "I'm concerned about creating access to capital" for biotech, he says. Milken won't discuss his net worth, but it has been estimated at nearly half a billion, with many Wall Street sources convinced that his vast portfolio of investments from his Drexel days make his real worth several times that. His family foundation's endowment alone is \$350 million.

Milken's blitzkrieg has both excited and unnerved a number of biotech companies who need money and currently don't see it coming from capital markets. With the industry in a deep slump, they're hoping Milken can reignite interest in these stocks. However, some bio-

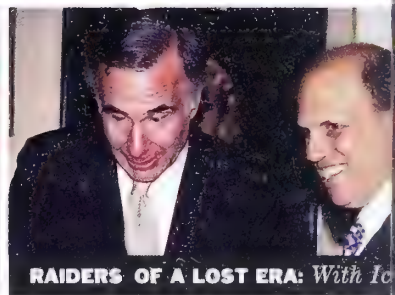
DEALMAKERS

MILKEN VS. CANCER

The millions of dollars the former junk-bond king is pouring into biotech are galvanizing—and worrying—the industry



BIG GUNS AT "21": With Cosby



RAIDERS OF A LOST ERA: With Ic

tech executives complain that Milken is mixing his profit and not-for-profit initiatives in ways that make them wary of getting too close. "He's trying to do what he did in junk bonds—[control] prostate-cancer research," complains one Silicon Valley venture capitalist.

FAMILIAR RING. Indeed, for those who watched Milken almost single-handedly catalyze a financial overhaul of Corporate America through the high-yield-bond network he ran from Drexel's Beverly Hills office in the 1980s, "creating access to capital" has a familiar ring. Milken's junk-bond network fueled corporate mergers and acquisitions by the score—and became symbolic of greed and excess when Milken pled guilty to securities-law violations in 1990.

Now, he's turning his capital, connections, business savvy, and sheer force of will to attacking prostate cancer. His impact already has been substantial: By

contributing more than \$9 million in direct-research grants through CapCure, Milken's family foundation now surpasses even the American Cancer Society as a sponsor of prostate research. At the while, everyone from a chorus line to the rich, powerful, and famous—including President Clinton, Senator Bob Dole, Larry King, Bill Cosby, Calvin Klein, and Carl Icahn—to staid academics have lauded his efforts, often at star-studded functions not unlike the Predators Ball Milken once hosted in Beverly Hills.

Says Dr. Samuel Broder, director of the National Cancer Institute, who will soon join biotech company Ivax Corp. "He has accomplished more than any of us had predicted, and we had high expectations to begin with."

Milken clearly is trying to save his own life here, not make money. For profits, he's banking on real estate and educational software. But he has to co-



HE MAY BE
IN A RACE
AGAINST
TIME



HEADS: With King



OBSESSION: With Klein

FUND-RAISING CapCure, Milken's prostate-cancer foundation, has given more than \$9 million to academic cancer researchers and has committed \$15 million more. A key strategy: money-raising soirees with celebrities such as Larry King and Bill Cosby.

PERSONAL INVESTMENTS Milken says that in 1995, he'll substantially increase his personal investments in biotech companies working in cancer research.

MATCHMAKING Milken is creating a network of supporters, including executives such as former Merck director Martin Wygod, in an effort to encourage large drug and chemical companies to merge with and support biotech outfits.

BIOTECH RESEARCH In September, Milken formed Cancer BioScience. In addition to its own research, it will contract out prostate-cancer work to academic labs. Respected Harvard researcher Lan Bo Chen is its scientific head.

threatened by the breadth of his efforts and by the blurry boundaries between them. The Milken family foundation, for example, currently bankrolls CapCure, which supposedly is focused on helping nonprofit, mainly academic researchers. Milken acknowledges, though, that CapCure also provided the funding to jumpstart his three-month-old for-profit company, Cancer BioScience.

That company is enigmatic, too: Although its scientific founder is respected Harvard University cell biologist Lan Bo Chen, its chief executive is Ralph Ingersoll II, one of Milken's old junk-bond customers who has no background in biotech or drug development (save a college major in chemistry). Ingersoll, who says he brings valuable perspective as an outsider, calls CBC a "virtual company" that primarily will tap into the best in academic-research labs. But Chen says it's also building a full laboratory and will buy advanced robotic screening equipment, both of which are capital-intensive assets that could pose a competitive threat to existing companies.

FRIEND OR FOE? No wonder some biotech companies are uneasy about whether to view Milken as a benefactor or competitor and about how much information to reveal to him. Dr. Phillip Frost, a former Sandoz Ltd. exec who briefly consulted with CapCure, thinks companies are "not foolish" to have concerns. Moreover, he says, "there are people involved [advising and working with Milken] who are amateurish." Milken says Frost had only brief involvement with his group, adding: "From day one, I said if people could not share information with each other, we couldn't share our money with them."

Researchers supported by Milken—those who will talk, anyway—tend to be wildly enthusiastic, not surprising given that money and a sense of urgency are like manna from heaven to academics used to scratching for support. And Milken seems remarkably relaxed, realistic, even philosophical. He has become a devotee of Eastern medicine, including meditation and special nutrition. And he says the time he spends with youngsters while performing court-ordered community service is part of "my therapy" for keeping things in perspective.

He'll need that. Cancer research is agonizingly slow compared with the world in which Milken made multimillion-dollar decisions in seconds. What are his chances of saving his own life? Impossible to say—but better since he started waging his own war on cancer.

By Joan O'C. Hamilton
in San Francisco

like other investors that they can make luck—and for that, the timing isn't ideal. Many biotech stocks are near their time lows, and liquidity prospects dim for hundreds of private companies. Milken's confidence is music to this eager industry's ears: "There are more exciting things going on in the biotech industry than the large pharmaceutical industry," he says.

Milken's footprints are everywhere in biotech, from scientific meetings to venture-capital firms to cutting-edge gene-therapy companies to Ivy League schools—not easy for a man whose probate terms require him to get permission to leave California. He has spent time with scientist-entrepreneurs and met with software billionaires Lawrence J. Ellison of Oracle Corp. and William H. Gates III of Microsoft Corp. to discuss ways they might contribute. The bad news: Not many companies

are even looking at prostate-cancer therapies. There's Somatix Therapy Corp., Ligand Pharmaceuticals, and probably only about a dozen others. The disease kills 38,000 each year, and 200,000 new cases are diagnosed annually. Historically, though, prostate cancer hasn't been considered a good commercial target because only about 10% of its victims get the fast-growing, virulent form that Milken appears to have. More often, it afflicts older men and is not always their cause of death.

Milken remains optimistic, however, because he realizes that breakthroughs could come from work on other cancers or from development of technologies not now directed at prostate cancer. Also, he has lost half a dozen close family members to a variety of cancers and wants to spark research across the board.

Companies respect Milken for not seeking a quick fix. But some also feel

GOVERNMENT

HERE A CUT, THERE A CUT...

Some pricey tax plans are on the table—but no budget-busters

The last time Washington caught such a case of tax-cut fever, the federal budget deficit soared, interest rates spiked, and the nation slipped into recession. But things were different in 1981. Today, even as the two parties compete to appease taxpayers, there should be no repeat of such troubles when the new Congress convenes.

What has changed this time around?

lessly cause the deficit to skyrocket," says Stanley Collender, chief budget analyst at Price Waterhouse.

Certainly, plans to cut taxes are beginning to snowball, just as in Reagan's first year. None was more dramatic than Clinton's abrupt about-face on taxes (table). The President elevated the popular sentiment for smaller government into an initiative—which he dubbed a

clusion for capital gains, which would be indexed for inflation. The cost: some \$149 billion over five years. And Senator Phil Gramm (R-Tex.), a leading 1996 Presidential contender, proposes doubling the current personal exemption for each child, to \$5,000—at a cost of \$124 billion over five years.

But this run on Fort Knox does not yet constitute a budget crisis. That's because no one in either political party has suggested tax relief without paying for the lost revenue with other tax hikes, user fees, or spending cuts. Such leavening was missing in Reagan's supply-side recipe.

"RECONCILIATION BILL." This time around, the White House insists deficit cutting is still a top priority. The Clinton Administration is drafting a five-year budget blueprint for fiscal 1996 that would show \$76 billion in spending cuts to offset \$60 billion in tax reductions.

Republicans plan to be far tougher. In a highly unusual move, incoming House Appropriations Committee Chairman Robert L. Livingston (R-La.) promises to slash spending in the current fiscal year to make a downpayment on future tax cuts. And new House Budget Committee Chairman John R. Kasich (R-Ohio) says he will craft a plan to balance the budget by fiscal 2002. That would match the promise of the Balanced Budget Amendment that House GOP leaders have made their first legislative priority.

More important, the vehicle for the GOP plan most likely will be a massive "reconciliation bill" that matches tax and spending changes dollar for dollar. That would impose discipline and keep tax cuts from swelling the deficit. In addition, it would allow the GOP to sneak a capital-gains-tax cut past a potential Presidential veto.

At this stage of the process, promises are cheap. Balancing the budget in 2002 would require \$1.2 trillion in cuts, anticipated spending—a virtual political impossibility. That's more than twice the size of the deficit reduction Clinton managed to get through the House and Senate in 1993. Those deficit-slashing heroics "would be a little skirmish, compared to what would have to be accomplished to balance the budget in several years," according to Leslie M. Alpert, an economist at NatWest Securities Corp.

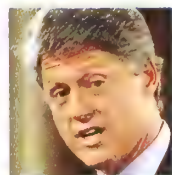
Still—whatever happens, it's unlikely that Congress can break the ban. The prognosis: The federal budget may yet recover from tax-cut fever without major complications.

By Paul Magnusson in Washington



TAX-CUT FEVER

The various tax-slashing plans being proposed to Congress and estimates of their five-year cost.



CLINTON A \$500 tax credit for children under 13 in families making less than \$75,000; a deduction of up to \$10,000 for post-secondary-school education for those with incomes below \$120,000. Plus, a new type of IRA to fund tuition payments, a new house, or care for the elderly. Cost: **\$60 billion.**



GINGRICH'S "Contract With America"—A \$500 tax credit for kids 17 and under for families making up to \$200,000; a 50% exclusion from capital-gains taxes, plus accelerated depreciation, credits for adoption expenses, and credits for home care for the elderly. Cost: **\$149 billion.**



GEHPARDT A \$300-to-\$600 tax credit for filers who earn less than \$75,000. Cost: **Unknown.**



GRAMM Double the current \$2,500 exemption per child, to \$5,000, with no income cap. Cost: **\$124 billion.**

Plenty: Budget rules and spending caps are forcing lawmakers to offset cuts with spending reductions. And the markets won't be lulled by phony accounting or promises that tax cuts will pay for themselves by spurring growth. After all, the amount of federal debt held by the investing public has quadrupled and gone global. "Given the attention of the financial markets to the whole budget process now and the concerns of the Federal Reserve on inflation, it's hard to believe that Congress would just mind-

middle-class "bill of rights"—that would cost an estimated \$60 billion over five years. Not to be outdone, House Minority Leader-to-be Richard A. Gephardt (D-Mo.) sketched out a \$300-to-\$600 middle-class credit of his own.

The GOP's plan, however, looms as the costliest by far. The Contract With America is laden with tax cuts—and not just for the middle class. A \$500 tax credit for each child 17 and younger would go to families making less than \$200,000. Investors would get a 50% ex-

By Christopher Farrell

A JUMBLE ONLY A FLAT TAX CAN UNTANGLE

Everything should be made as simple as possible, but not more so.

—Albert Einstein

With both Republicans and Democrats grasping wildly for the middle-class vote, federal tax reform seems virtually certain in 1995. We may finally witness a slashing of the capital-gains-tax rate, a deduction for losses on home sales, a \$500-per-child tax credit, and an expanded individual retirement account.

Yet these steps and others only promise to impair further a tax code riddled with too many exemptions, deductions, exclusions, and credits. If Washington legislators truly want to make a difference, they should head the other way and embrace a flat tax.

A flat tax? The very idea, which would mean doing away with most exemptions, is generally dismissed out of hand as political suicide, despite such vocal backers as Richard K. Arney (R-Tex.) in the House. But it makes sense—far more than any other reform being considered. Limiting exemptions and deductions would lower the tax rate by broadening the tax base. And the change would encourage a more efficient allocation of resources—not least by reducing government interference in citizens' financial choices. **TEN-YEAR-OLD PLAN.** What exactly would a flat tax entail? A good starting point is the one that was proposed by Hoover Institute economists Robert E. Hall and Alvin Rabushka about a decade ago. They would have levied a single 19% tax on wages and salaries, with personal and dependent exemptions retained to keep the scheme somewhat progressive. Capital gains, interest, and dividends would be exempt. And

businesses would pay the same 19% rate, with no deductions for interest or dividend payments.

If that's too much for voters, there are more moderate alternatives. Around the same time Hall and Rabushka formulated their approach, the Bradley-Gephardt plan offered three brackets: 14%, 26%, and 30%, with a few of the most popular deductions preserved, such as home-mortgage interest and charitable

fling for tax reasons, too. With a simple tax system, taxpayers would make their own investment decisions without government telling them which assets or time period to favor. **MUCH-NEEDED STABILITY.** Other advantages: The so-called tax gap—the estimated \$120 billion in tax revenue not collected by the Internal Revenue Service because of underreporting of income or overstating of deductions—likely would shrink if

taxes became simple to calculate. Such a system would also promote much-needed fiscal stability. In his 1962 book, *Capitalism and Freedom*, Milton Friedman (who proposed a 17% flat-rate tax) argued that lurches in the tax code create random disturbances in the economy, disrupting investment and other financial plans. Just think of all the shifts in tax policy during the Reagan, Bush, and early Clinton years. A flat tax would have an effect on fiscal policy sim-

ilar to the pursuit of a consistent monetary policy: It would work to minimize economic disruptions.

Most important, a flat tax would separate revenue-raising from policymaking. Today, too many government programs and key economic policies are buried in the tax code. That makes for bad policy and inefficient taxes. Far better to remove tax-code fiddling as an option for policymakers and keep any fiscal-policy debate focused on government expenditures. What government programs do we want, and how much are we willing to spend for them? Radical reform, if it finally arrives, will help us get a better feel for the scale and scope of our government—and for what we want it to become.

Farrell writes on economics.



contributions. "You want to maintain progressivity in the system," says co-author Senator Bill Bradley (D-N.J.). "And some exclusions and deductions are so embedded in the way business is done that the battle wouldn't be worth fighting."

Radical tax simplification might have a better chance of passing if its economic benefits were better understood. The cost of complying with tax rules is huge, for one thing. For individuals alone, the tab comes to more than \$30 billion per year, says Joel B. Slemrod, an economist at the University of Michigan at Ann Arbor. A flat tax, which is much simpler to calculate and process, would eliminate the need for so many tax lawyers and accountants while thinning the Internal Revenue Service's bureaucracy. There would be a lot less asset-shuf-

*It would be cheaper, fairer, less wasteful
—and more efficient for Uncle Sam*

LEGAL AFFAIRS

CAN THE GOP STOP THE MEGA-VERDICTS?

The party wants to limit awards, but "it's not a slam dunk"

Call it Dan Quayle's revenge. The former Vice-President made little headway while in office in his campaign to modernize the nation's tradition-encrusted legal system. Now, Quayle is back in Indiana—but his lawyer-bashing crusade has been resurrected by a Republican-led Congress.

GOP lawmakers see reform as part of a broader mandate to restore a measure of individual responsibility. Voters want limits on lawsuits run amok, because "we've gone overboard in saying everyone's a victim," says GOP pollster Steven Wagner at Luntz Research. Republicans are also playing to corporate interests that want to cut the cost of regulation and litigation.

GRIPES. The focus of the GOP's attack is its Common Sense Legal Reform Act, to be introduced in the House on Jan. 4. The bill would limit damages in product-liability cases, make it tougher for shareholders to sue companies, and discourage suits by forcing losers to pay winners' legal costs.

It's an agenda business has sought in vain for 14 years. Although courts often scale back mega-verdicts, executives gripe that the threat of huge awards boosts settlement costs. "The numbers are in the stratosphere," complains Monsanto CEO Richard J. Mahoney. Meanwhile, foreign rivals aren't saddled with the same costs. The failure to adopt reform in the U.S. "places American companies at a substantial disadvantage," says Larry E. Sanford, executive vice-president of MacAndrews & Forbes Holdings Inc.'s Coleman Co. unit.

Legal reform still faces plenty of barriers. Opponents, from consumer groups to the well-heeled Association of Trial Lawyers of America, plan to launch a

bruising counteroffensive. And Republicans themselves aren't united: Some Senators, including Alfonse M. D'Amato (R-N.Y.) and Alan K. Simpson (R-Wyo.), have sided with reform opponents in the past. Business, meanwhile, frets that the Republicans' more radical proposals will drive away votes. "It's not a slam dunk," says business lobbyist Mike House.

But the GOP thinks its plan will resonate with voters. A postelection Gallup Poll revealed that 58% of the public fa-

Ultimately, opponents likely will seize on the controversial proposal that would force losers in specified federal cases to pay all legal expenses. Some companies fear the issue will derail the reform drive. The requirement doesn't have a snowball's chance in July of seeing the light of day," says Kevin Condon, assistant general counsel for litigation at Sears, Roebuck & Co.'s merchandising unit. And critics add the provision wouldn't stop plaintiffs from filing frivolous litigation in state courts.

LITMUS TEST. Quayle-style legal reformers, however, view the loser-pay principle as a political litmus test. Business "kept trying to compromise with the liberals," complains freshman Representative David M. McIntosh (R-Ind.), a former Quayle aide. "Now that the Republicans are in, we should go back to the right ideas." Other Republicans hope to flush out expected opposition from

LAWYERS BE DAMNED

Key features of the GOP's legal reform plan

PRODUCT LIABILITY The proposed legislation would limit damages paid by companies sued for injuries caused by their products. Punitive damages would be held at the greater of three times actual damages or \$250,000.

SHAREHOLDER CLASS ACTIONS Plaintiffs would be limited to five securities class actions a year and would have to show their losses resulted from intentionally misrepresented information from companies.

CIVIL JUSTICE SYSTEM To discourage people from bringing baseless cases, the losers in some federal lawsuits would have to pay the winners' legal costs.

vored legal reforms, with only 28% opposed. "When people read about these multimillion-dollar verdicts in the newspaper, they're beginning to realize that in a subtle way, it [costs] jobs," says John S. Breed, manager of civic affairs for Cooper Industries Inc.

Opponents think popular sentiment will shift when they demonstrate how the GOP proposals would curb the rights of the injured. In suits claiming damage from defective products, for instance, awards would be limited to triple out-of-pocket costs or \$250,000, whichever is greater. Voters in Arizona and Michigan already have defeated ballot initiatives calling for similar caps.

the two-lawyer First Family, which has been quiet on the issue. The President received \$500,000 in contributions from trial lawyers in the 1992 campaign.

Most CEOs, however, would be content with compromise legislation limiting punitive damages and ending the practice of holding companies fully liable for injuries they only partially caused. With key votes looming before April, Corporate America will know soon if the new GOP leadership is more interested in providing relief from excessive litigation—or in scoring political points.

By Catherine Yang in Washington with bureau reports



TENSION AND TAUTNESS' IN THE TAURUS—AND AT FORD

The redesign looks great, but will buyers pay the extra freight?

There's no denying that the new Ford Taurus and Mercury Sable are stunners. Unlike 1991, when Ford rejiggered the two with new body panels, this year's redesign is almost total. The '96 models have a sculpted, "bio-kinetic" look that Ford is betting will be as distinctive—and successful—as the original "aerodynamic" design. "We aimed for a tension and tautness in the surface to express the energy beneath the surface," says John J. Telnack, Ford Motor Co.'s vice-president for design. Translation: The cars' curving body metal is meant to appear to be always in motion.

Ford has a lot at stake in making the new Taurus/Sable—scheduled to hit the showrooms this summer—a success. Theplings helped lead the company's renaissance: They account for a quarter of Ford's new-car sales (chart): 330,984 Taurus and 112,227 Sables were sold the first 11 months of 1994. And for three straight years, the Taurus has been America's top-selling model, besting Honda Motor Co.'s Accord.

SWITCH. Yet Ford paid a price for the redesign that goes well beyond its \$9 billion estimated cost. Although the new Taurus/Sable's parts are individually easier to assemble than their predecessors', the sheer number of features Ford has added—everything from gimmicky multi-purpose center consoles to optional filter to winnow dust and pollen out of the air—means they take longer to build. That's a major reversal of the industry's trend toward cars that are easier, quicker—and cheaper—to make.

Ford won't take the kudos off the Taurus until Jan. 3, but changes in the Sable give an idea of what's coming in both models. Indeed, the two are most mechanically alike. Gone from the Sable is the distinctive "light bar" that wraps from headlight to headlight: The headlamps are now elliptical ovals. Inside is elliptical, all-in-one

instrument cluster on the dash, with large controls laid out ergonomically. Other features include an optional 3-liter, multivalve V-6 engine capable of going 100,000 miles between tune-ups and a glove-box door on damped hinges so it won't fall on a passenger's knees.

Sticker prices on the Taurus and Sable won't be set until shortly before the cars appear. But Christopher W. Cedergren, an analyst at market researcher AutoPacific Group in Santa Ana, Calif., figures that their base prices will go up 6% to 8% from the Taurus' current \$17,585 and the Sable's \$18,210. That would push them higher than an Accord LX 4-Door, which now has a base price of \$17,750. "Ford is really playing a high-stakes game with its price increases this year," says David E. Cole, director of the University of Michigan's Office for the Study of Automotive Transportation.

Other examples: The sticker price of

its redesigned Explorer is up, and its all-new 1995 Lincoln Continental, developed about the same time as the Taurus and Sable, has a new base price of \$41,375, a \$7,000 increase.

How did the new Taurus and Sable end up so complicated to build? Richard L. Landgraff, head of development, admits his group had an ambitious target: "to benchmark the best and reinvent a car with the market impact of the original Ford Taurus." But Landgraff also notes that in mid-1992, when the team members were putting together their wish list, they could feel the

Japanese breathing down their necks. The Accord had outsold the Taurus by 100,000 units in 1991. And Toyota Motor Corp. had just come out with a feature-laden version of its popular Camry sedan.

As it turned out, 1992 represented a crest of Japanese overengineering. Now, Japanese rivals are trying to

cope with the sky-high yen by removing engineering flourishes and features. For instance, Honda simplified the Accord when it was redesigned for the 1994 model year, keeping its cost and price the same as for its forerunner. And Toyota has vowed to slash costs by 20% for all new models—including a totally revamped Camry it plans for the 1997 model year.

Ford, of course, didn't let costs get totally out of line in its Taurus and Sable redesign. The Sable no longer has rubber side moldings running its length with "Sable" inscribed. That alone probably saves more than \$100 per car, says AutoPacific Group President George C. Peterson.

And Ford may yet find other economies to bring the cars in at less than analysts' price estimates. If it doesn't, bio-kinetic could come to mean "looks fast even when it's not moving fast... off the dealer lots."

By James B. Treece
in Detroit



The sculpted look is a far cry from the earlier Taurus and Sable



SABLE: SLEEK SISTER

TAURUS AND SABLE: FORD'S BREAD AND BUTTER

SHARE OF FORD'S TOTAL NEW-CAR SALES

DATA SOURCE: AUTOMOTIVE NEWS

'92 '93 '94



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News: Analysis & Commentary



LOOK MA, NO HANDBOOK:
Fries with the guest of honor

er market. Computers may have been among the hottest holiday gifts this year, but most American homes still don't have one. With Bob, Microsoft aims to help remedy that. The product's most novel feature may be what it lacks: an instruction manual. Instead, it offers on-screen characters, each with a personality, that volunteer advice and steer users through the programs.

TINY TUTORS. Bob is actually a suite of programs, including a letter-writing aid, a checkbook, and a program to keep schedule. When users log in

SOFTWARE

MICROSOFT: HE-E-E-RE'S BOB!

Its program for computerphobes may live up to the hype

Just who is Bob, anyway? At the Consumer Electronics Show in Las Vegas, which starts on Jan. 6, visitors will be inundated with his grinning face on billboards, posters, napkins, and balloons. His coming-out party is being managed by the royal couple of the computer industry, Microsoft Corp. Chairman William H. Gates III and his wife, Melinda French. A marketing manager at Microsoft, French is set on making sure we all get to know Bob, a new Microsoft program.

Why the hoopla? Set to hit stores on Mar. 31, Bob is Microsoft's attempt to lure computerphobes into the market with a "social interface"—a new way to interact with PCs. "The social interface is the next step in computing," asserts Karen E. Fries, Microsoft's program manager in charge of creating Bob. The software design is based on a theory by Stanford University professors that aims to make using a PC as easy as if you had an expert looking over your shoulder. It's likely to start a new battle as software and PC companies vie for ways to move beyond the current Windows-style "graphical interface" and appeal to the average computerphobe.

Microsoft's main aim is to make greater inroads into the home-comput-

with a personal password, they see an image of a room on the computer screen which they can customize. You can call up your personal calendar, for example, by clicking on the calendar on the wall. If you have questions, you click on the guides that are always present on the corner of the screen. As time goes on, the helpers learn your preferences and level of ability, to better judge when they should pipe in with advice.

Outsiders who have tried the program give it high marks. Most find it even easier to use than Apple Computer Inc.'s Macintosh interface, widely regarded as the easiest to use among today's offerings. "It blew me away," says William M. Bluestein, an analyst with Forrester Research Inc.

That doesn't mean Bob will be an instant success. The social interface will work only on the suite of programs specifically bundled into the program, at least for now. And as a suite of eight very simple programs, it may be overpriced at \$100. Moreover, because of its many features, Bob is slow unless used on the most powerful computers.

Yet another potential problem: resistance from computer makers. Most aren't talking, but Forrester's Bluestein says many of them are reluctant to endorse the product because they offer their own add-ons to make Windows easier to use.

Nevertheless, Bob is an important first step in the next battle for the software industry. Apple, for one, has a couple of new interfaces in the works, the first one scheduled to debut about a year from now. It will just have to hope that Microsoft hasn't made Bob a household name by then.

By Richard Brandt in San Francisco

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STRATEGIES

RED ALERT AT FIRST ALERT

It faces a PR disaster over its highly sensitive CO detectors

When the First Alert carbon monoxide detector in Daryl Wyatt's Chicago apartment went off at 5 a.m. on Dec. 21, he rushed his family to a neighbor's and called the fire department. While waiting outside, he saw fire trucks careening in all directions, "but they kept going past our house."

Small wonder. The Chicago Fire Dept. answered an unprecedented 1,852 false alarms that night from carbon monoxide detectors—most of them First Alert's. The chaos was blamed on a weather condition that trapped fumes close to the ground, but even Mayor Richard M. Daley criticized First Alert's detectors.

Now, alarm bells are ringing at First Alert Inc.'s Aurora (Ill.) headquarters. Sales of its detectors in Chicago, once boosted by a city ordinance, have slowed



PULLING THE PLUG: Was the product too good?

dramatically, and smaller competitors are beefing up advertising to win market share. The company had already pulled a planned \$125 million secondary offering in December following reports of overstatements in its prospectus—which the company denies—and its stock is down 25%, to around 14.

On Dec. 22, First Alert conceded its product could be improved and offered a refund to Chicago area customers. But the damage was done. Only nine months ago, First Alert—best known for its pop-

ular smoke detectors—was one of the hottest initial public offerings around. With widespread name recognition and distribution clout, it captured 70% of the fast-growing CO detector market. Profits in the first nine months of 1994 were up fivefold, \$8.7 million, on sales of \$148. million.

NEW BUTTON. The problem with First Alert's detector was in essence, too good. The company designed its product to go off at very low levels of CO. And unlike rivals' products, which are easily

reset, First Alert's detectors must be placed in a CO-free environment above 40F for as long as 48 hours after they've gone off. The company won't have an improved version with a fast-reset button ready until later this year.

First Alert's majority shareholder, financier Thomas H. Lee, says the debacle "is obviously a public relations setback but we don't think the financial impact will be significant." Still, the company has to stop the alarm bells in Chicago.

By Susan Chandler in Chicago



TOKYO, September 1, 1923. The Imperial Hotel's new Frank Lloyd Wright building was finally opened. And then, midway through the celebrations, the Great Kanto Earthquake struck. Within hours, The Imperial was overrun by refugees. We ran out of rooms, so we put them in the Grill. We ran out of food, so we served rice gruel. We had no lights, no heat, no phones. But we also had no complaints. Much later, a cablegram reached the architect in California: "HOTEL STANDS UNDAMAGED AS MONUMENT TO YOUR GENIUS. HUNDREDS OF HOMELESS ASSISTED

BY PERFECTLY
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STEAMY SITCOM: *Muscle*, set in a gym, will debut on Warner Bros. network

TELEVISION

ARE PARAMOUNT AND WARNER LOONEY TUNES?

Their new nets must grab young viewers from entrenched rivals

It's always been a holy grail for network executives. But the search for young, spendthrift viewers is likely to hit a new high—or low—in mid-January. That's when two of Hollywood's most powerful studios, Time Warner Inc.'s Warner Bros. and Viacom Inc.'s Paramount Pictures, will roll out networks-in-training designed to outfox Fox, the network that has made its mark with edgy, racy shows such as *Married... with Children*, *Cops*, and *Melrose Place*.

Ready for shows featuring a lesbian TV anchorwoman and a rash of exploding cars? WB Network and United Paramount Network, which will debut on Jan. 11 and 16, respectively, sure hope so. Even though networks are back in vogue and making money again, launching a new one is a hugely expensive gamble against entrenched competitors—especially when your game plan is to target fickle young viewers.

The opportunity certainly is clear: Warner and Paramount Communications Inc. both hope to create captive, brand-name distribution outlets for programs they produce and buy, just as Fox did for Rupert Murdoch's News Corp. Viacom, which is expected to announce soon that it has sold its cable properties for \$2 billion, needs to build up a system of TV stations to ensure distribution for shows

made by Paramount. And Time Warner, which backed off a deal to buy NBC Inc., wants an outlet for its TV shows and huge library of Looney Tune cartoons.

But Fox and TV's Big Three aren't exactly quaking in their Guccis. Neither newcomer will start with more than four hours a week of prime-time shows. And they'll be broadcast over a makeshift lineup that includes UHF stations, affiliates borrowed from other nets, and cable.

As far as it goes, both will offer network-quality programming: United Paramount Network will open with its third *Star Trek* spin-off, while Warner's four sitcoms will include entries from producers who created such hits as *In Liv-*

ing Color and *Soap*. But while the new nets will have affiliates in 80% of the country and most major markets, there will be plenty of folks who won't know they're around. Viewers in three dozen markets will have to catch *Star Trek: Voyager* late at night or on weekends because the only stations Paramount could line up were already Fox affiliates. Warner will rely on Tribune Co.'s WGN superstation to carry its programming to 18% of its viewers.

With *Star Trek* and a marginally better station lineup, industry experts predict Paramount will get out of the box more quickly. But both newcomers are likely to lose \$50 million a year or more for years, figures Oppenheimer & Co. analyst Jessica J. Reif. "It's a three-, four-, five-, maybe six-year project," says WB Chairman Jamie Kellner, who guided Fox through its first eight years and owns a piece of the Warner network.

TESTOSTERONE TV. Both networks are clearly modeling themselves after Fox, which overcame hefty losses itself and this year earned \$300 million with its network and TV stations. UPN President Lucille S. Salhany and other executives at the nascent networks hail from Fox. And the new shows have much of the Fox edge that plays well with a younger, urban audience. Paramount, looking for young male viewers, will unveil an action show from *A-Team* creator Stephen J. Cannell. Warner's offerings include *Muscle*, a sitcom about life at a gym that includes the gay anchorwoman.

Will testosterone TV and Generation-X fare sell advertising? Both networks claim they've sold out all the ads they

intend to sell in their first season, though each has liberally held back spots to give free to advertisers in case audiences are lower than expected. Their sales were helped by a robust ad market, and the newcomers have significantly undercut the \$11 to \$12 per thousand viewers that the Big Four charge, with Warner asking \$7.50 and Paramount \$8.25.

Survival, however, depends on keeping young viewers glued to the screen. Even the new networks are counting on a high casualty rate. "We're betting that this is a five-network world, with only one of the two likely to make it," says Kerry McCluggage, chairman of Paramount's TV group. Survival of the fittest: That's as stirring as TV high drama gets.

By Ronald Grover in Los Angeles



UNITED PARAMOUNT'S LOGO

TV on the Cheap

	AD COST/ THOUSAND VIEWS	30-SECOND AD PRICE*
ABC	\$12.00	\$139,200
FOX	11.00	75,900
UNITED PARAMOUNT	8.25	24,000
WB TELEVISION	7.50	20,000

*Based on actual or projected viewers DATA: BUSINESS WEEK

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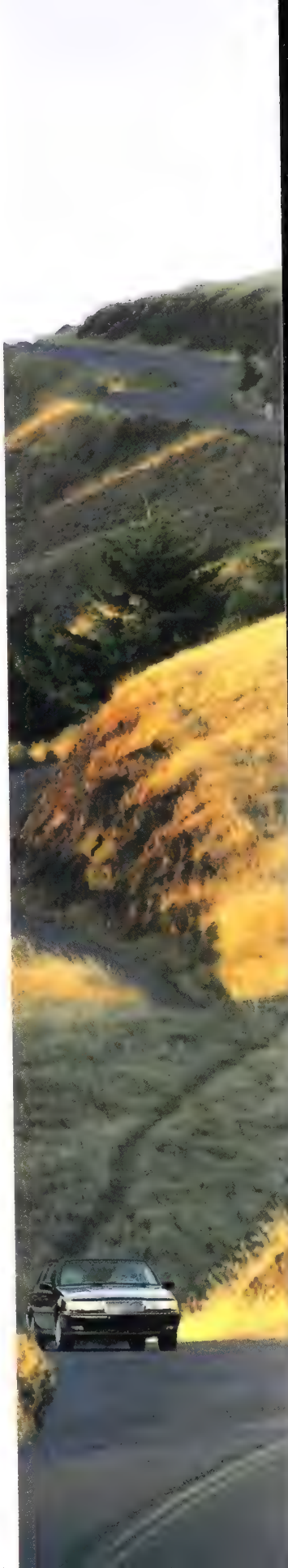
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VOLVO

EDITED BY KEITH H. HAMMONDS

ARASKOG'S BIG DEAL OR ITT

AND ARASKOG HAS DRAWN plenty of flak for running an unwieldy conglomerate with a fuzzy focus and weak strategy in his 15 years at the helm of ITT. Now, he seems to be trying to remake his big company before he retires in 1996. On Dec. 27, ITT announced its plan to sell parts of its Financial to Norwest, Deutsche Bank North America and a third buyer, for up to \$7 billion in all. That would help pay for its Dec. 19 deal to buy Caesars World for \$1.7 billion. Investors pushed ITT stock up 5.2%, to 88%, on the news. That can't hurt Araskog,

CLOSING BELL

MEGAFLOP?

Cray Research, maker of ultrafast computers, was too slow to remake itself. On Dec. 1, CEO John Carlson abruptly resigned. The stock fell to 15, a wisp of the 135 it traded at in 1987. Cray's supercomputers have lost ground to microprocessor-based machines. Cray sells those, too, but at lower margins and against brutal competition. Earnings will be down this year, and Cray expects a flat 1995. Officially, the board says Carlson wanted to retire. But the decision came at a special board meeting—three weeks after Carlson apprised it of his 1995 strategy.



who could pocket \$18 million in stock gains and options if ITT shares reach 118. Analysts expect Araskog to spin out the fast-growing \$4 billion-a-year entertainment unit.

TELEDYNE INVESTORS AREN'T ALTAR-SHY

TELEDYNE MAY HAVE UNEquivocally turned down steelmaker WHX's recent \$1.2 billion takeover bid. But some investors are getting antsy. "We would strongly encourage the company to at least sit down and explore the possibility" of a sale, says Gerald Cramer, whose Cramer Rosenthal McGlynn holds a 1.5% stake in Teledyne. One source close to the deal predicts Teledyne's rebuff of WHX Chairman Ronald Labow may backfire, sparking a bidding war with other corporations eyeing Teledyne's \$1.9 billion pension assets. "We were surprised. We thought the door was open" to WHX's bid, says one Labow adviser.

IS PICKENS' MESA TAKEOVER PICKINGS?

HAS MESA, LED BY ONETIME corporate raider Boone Pickens, become takeover bait? Mesa revealed on Dec. 21 that Montana millionaire Dennis Washington had taken nearly a 5% stake and may raise his holdings to over 25%. What's more, Washington's adviser is David Batchelder, once Pickens' top takeover strategist. Even without pressure from Washington, Pickens is aiming to boost Mesa's ailing stock by selling most or all of the company's crown jewel, its Hugoton natural-gas properties in Kansas, to pay off debts.

LORENZO MAY HIT THE SILK

FRANK LORENZO'S ILL-FATED new airline, ATX, may try again

HEADLINER

SAATCHI AFTER MAURICE SAATCHI

When the end came, the leader of the coup that ousted adman Maurice Saatchi from the chairmanship of Saatchi & Saatchi was enjoying his 34th birthday scuba-diving in the Caymans. But David Herro (right), who heads the \$1.2 billion Oakmark International Fund, says there was no rejoicing when Saatchi was toppled on Dec. 16 after a bitter board meeting. "We'll celebrate when the stock doubles," says Herro, whose fund owns 9.5% of Saatchi.

Herro bought Saatchi shares when he helped start Oakmark two years ago, betting the agency would turn

around after a financial restructuring. But he grew alarmed in early 1994 when a feud broke out between Maurice Saatchi and Saatchi CEO Charles Scott, in part over Scott's moves to rein in spending. In the fall, Herro began marshalling fellow shareholders on word of a scheme to give Maurice Saatchi \$8 million if Saatchi shares doubled over three years.

The victory may have a downside if clients such as candymaker Mars exit with Saatchi. Herro contends that the chairman's presence was "crippling." He has a lot riding on that assessment.

By Richard Melcher



to get off the ground—but perhaps without Lorenzo. The former Continental Airlines chairman says he's considering selling all or most of his 23% stake in ATX. This in the wake of a ruling by the U.S. Court of Appeals for the District of Columbia Circuit upholding a Transportation Dept. decision that his company was unfit to operate an airline. The decision "certainly rules out over the near term a major financial role in any U.S. aviation venture," says Lorenzo. He wouldn't comment on reports that he's working on an airline deal in India and advising several European carriers.

GLAD TIDINGS FOR TINSELTOWN

DUMB SELLS. THE SLAPSTICK Jim Carrey film, *Dumb and Dumber*, helped Hollywood take in \$91.3 million at box offices over the four-day Christmas weekend. After strug-

gling for weeks to lure folks away from shopping malls, the industry is now \$65 million ahead of last holiday season, figures the trade newspaper *Hollywood Reporter*. And with strong late-year results for such hits as Tim Allen's *The Santa Clause* and Jean-Claude Van Damme's *Street Fighter*, ticket sales for the year appear likely to hit a record \$5.4 billion. Among the holiday losers: Fox's *Miracle on 34th Street* remake and Paramount's *Mixed Nuts*.

ET CETERA...

- Baseball in April? Don't count on it. The owners imposed a player salary cap.
- Christmas sales were fairly merry—except for apparel retailers and Toys 'R' Us.
- Troubled Merry-Go-Round will shutter 200 of its 1,200 clothing stores by February.
- Upjohn halted trials of Freedox, a trauma drug, because of a high death rate.

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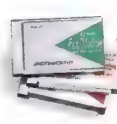
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EDITED BY STAN CROCK

OLD MacDONALD HAS A SUBSIDY— AND THE GOP HAS A DILEMMA

They swept to power on Nov. 8 by pledging to take a pitchfork to hundreds of wasteful federal programs. But Republican budget-cutters may have unexpected trouble naming a key target: a farm bill chock-full of the uneconomical subsidies they claim to loath. The GOP is split over the program, with some lawmakers defending the aid and others wanting to pare it to finance promised tax cuts.

The early betting is that farmers and such agribusiness giants as ConAgra Inc. and Cargill may fare better than other GOP targets. Unlike welfare chiselers, farmers are a core party constituency. And Senate Majority Leader Bob Dole (R-Mo.) doesn't plan to launch his Presidential campaign in Iowa as the man who plowed the nation's wheat fields.

That won't stop some budget hawks from making a run at the subsidies, of course. Senate Agriculture Committee Chairman Richard G. Lugar (R-Ind.) says he'll consider ending some subsidies to meet the GOP goal of slashing at least \$170 billion from federal spending. And incoming House Majority Leader Richard K. Armey of Texas, who will be right-hand man to Speaker Newt Gingrich, promises "major changes" in the 1995 farm bill.

TAB. Savings could be substantial. Lugar notes that crop subsidies and disaster relief will soar to \$58 billion between 1991 and 1995, \$17 billion more than estimates issued in 1990 when supports were last pared for rice, corn, cotton, and other crops. The tab is up largely because bumper harvests hurt prices, forcing Washington to pay more to meet price floors. These programs have been out of control," gripes Lugar. But some powerful Republicans are less enthusiastic about wielding a scythe. Both Dole and House Agriculture Committee Chairman Pat Roberts are dedicated farm champions from Kansas. Dole recently wangled concessions from the White House to protect farmers in exchange for his support

of the General Agreement on Tariffs & Trade. What's more, on Dec. 28, the Administration named a moderate, former Representative Daniel R. Glickman (D-Kan.), as Agriculture Secretary. He won't advocate tilling under all subsidies.

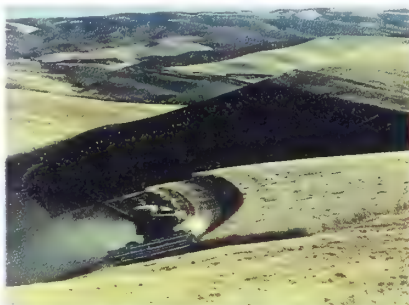
BUSTED BANKS? The farm lobby also will be working hard to foil reforms. The American Farm Bureau Federation contends that abrupt program changes could endanger the nation's food supply. Another claim: Pulling the plug could spark a financial upheaval, since the value of rural land used as collateral for bank loans is tied to subsidies. "The banks would be busted," warns Archer-Daniels-Midland Co. Chairman and CEO Dwayne O. Andreas.

The program's critics brush aside such scare stories. The Heritage Foundation, a wellspring of free-market ideas, will soon issue a report saying that America's rural areas would prosper, not suffer, under a market system. The think tank advocates eliminating subsidies that prop up crop prices and repealing burdensome rules such as pesticide regulations.

Democrats, meanwhile, are sitting on the sidelines, gleefully watching the GOP's agri-agonies. They see the Republicans facing two unpalatable choices: alienating loyal constituents or ducking real reform and earning the tag of hypocrites. "How can Republicans be for the free-market system everywhere except agriculture?" asks Representative Barney Frank (D-Mass.).

Ultimately, Republicans may finesse the farm fight by phasing out subsidies slowly. And they may limit the initial reform to peanuts and sugar, crops that are protected by quotas. That would provide convenient cover for the wheat farmers represented by Dole and Roberts. But it would give Democrats a bushful of political rejoinders when Republicans call for killing off outmoded New Deal programs.

By Mary Beth Regan



HARVEST TIME: Bumper subsidies

CAPITAL WRAPUP

EXPORT BOON

Commerce Secretary Ronald H. Brown is trying a new tack to promote American exports: handing out grants to trade associations. The Health Industry Manufacturers Assn. recently received a \$420,000 federal grant to help American makers of medical equipment get a toehold in Asian markets. HIMA will work with Asian health officials to design health-care systems. By getting in early, the group hopes to shape regulations that will benefit American manufacturers at the ex-

pense of their Japanese and European competitors.

ANOTHER LABOR LOSS?

► Business efforts to create worker-management committees could get a boost in the next Congress. In 1993, the National Labor Relations Board nixed panels dealing with such issues as working conditions, saying they amounted to sham unions. But labor committees in both houses plan bills that would clarify what issues worker-management committees may legally consider. Unions oppose the moves.

STARR'S SPACE EXPANDS

► The office of Independent Counsel Kenneth W. Starr is one federal bureaucracy that isn't shrinking. When Starr's people signed a lease in Little Rock in April, only a quarter of the 8,955 square feet they rented was empty, so many staffers moved into the local FBI office. This month, Starr's minions will move into the additional 6,724 square feet. The lease expires May 14, 1996—meaning the Whitewater inquiry could extend deep into the Presidential primary season.

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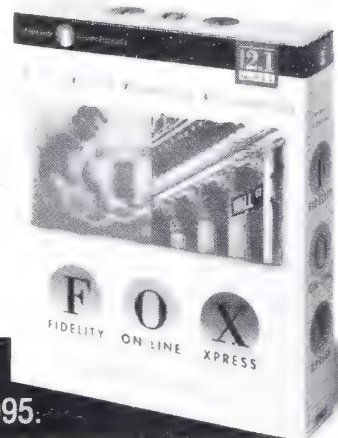


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EDITED BY CHRISTOPHER POWER

POLITICAL PANDEMONIUM COULD FRACTURE ITALY'S ECONOMY

Although it has had 53 governments since 1946, Italy has often prospered no matter what the politicians in Rome were up to. That has been the case since media tycoon Silvio Berlusconi cobbled together an unwieldy coalition to win national elections last March. The Italian economy has gone from strength to strength even as Berlusconi's government started crumbling. A weak lira coupled with a European recovery have pumped adrenalin into Italian exporters, while low peace and low consumer demand have beaten inflation to the lowest level in a generation.

This time, though, the political chaos could bring the party to a crashing end. A no-confidence motion put forward by Berlusconi's one-time ally—Umberto Bossi of the Northern League—forced the Prime Minister to submit his resignation on Dec. 22. Now, it could take weeks for Italian President Oscar Luigi Scalfaro to assemble a new government majority—possibly still led by Berlusconi's Forza Italia movement—or call for new national elections. Either way, Rome's fractious politicians will be wasting time squabbling just when Italy's financial health desperately needs attention.

RUNNING FOR COVER. The problem isn't the economy, it's the government's inability to reduce its debt load, now \$1.2 trillion and growing. The Berlusconi team had initially prepared a tough 1995 budget. But then, weakened by scandals and internal dissension, it caved in to union opposition to planned cuts in pension spending. Now, it looks as if government revenues will come up way short in 1995. As a result, planners have to start thinking about a supplementary budget to fill a new revenue gap of at least \$15 billion.

Investors have been running for cover. In Lugano, the Swiss border town just 48 miles from Italy's commercial capital, Milan, banks have been staying open Saturdays to cope with high demand from Italians bringing cash out of the coun-

try. Since January 1994, political jitters have sent more than \$70 billion in assets out of Italy. Meanwhile, the lira has lost more than 10% against the German mark since Berlusconi took office, while Milan's bourse has lost almost one-quarter of its value. And an increase in interest rates, now 12% on medium-term government bonds, means Rome must shell out an extra \$1 billion every month to service the country's debt. "The recovery of the economy is now dramatically at risk," warns Luigi Abete, head of the powerful Italian employers' federation, Confindustria.



BERLUSCONI: *Coming back?*

Further panic over Italy's ability to stabilize its national debt—now 120% of the gross domestic product—could spread beyond the Alps. "An Italian default," says Francis Scotland, managing editor of Montreal-based *Bank Credit Analyst*, "could set off a chain reaction, since investors would focus on other industrialized countries with critical ingredients for a default." Although Italy's budget crisis is the most acute, the public finances of Sweden, Canada, Greece, and Belgium are all in a precarious state.

PATCHWORK. There could be a benefit in this chaos. The breakdown of the Berlusconi government adds to pressure on Italy's politicians to move away from their unstable pattern of patchwork alliances toward a more traditionally European system of center-right and center-left.

Curiously, Berlusconi or a successor may benefit from this realignment. A new conservative candidate may be able to forge a more cohesive, broad-based party to beat the former communists in a possible election.

A disciplined party might prove capable of containing the debt crisis, facing down the unions, and calming the markets. The big question is whether Italy's economy can avoid paralysis until the political air is cleared.

By John Rossant in Rome

GLOBAL WRAPUP

BID-RIGGING PROBE IN JAPAN

Japan's Fair Trade Commission (FTC) will probably soon file criminal charges against nine electronics companies for rigging bids in public-works contracts. Executives at Hitachi Electronics, Toshiba, Mitsubishi Electric, Fuji Electric, and Meidensha allegedly conspired with four smaller outfits to divide up \$500 million in contracts that are handed out annually by the Japanese Public Works Agency. That would violate the antimonopoly laws, which American negotiators are pressing

Japan to enforce more vigorously to force Japanese markets open to U.S. corporations. The companies deny the allegations. The case would be the third one that has been brought by the FTC since 1990.

CELLULAR PHONES IN ISRAEL

► The cellular-phone monopoly in Israel has come to an end. On Dec. 27, CellCom, a company formed by America's BellSouth, Israel's Discount Investment, and the Brazilian branch of the Safra family started offering cellular-phone service. Until now, the coun-

try's 150,000-strong cellular-phone network was operated exclusively by Israel's Bezeq Telecommunications Co. in a joint venture with Motorola Inc. CellCom claims that its digital network will be the cheapest in the world for consumers. Demand for the company's telephones was so great on the first day of operations that police had to be called in to restore order at several of the company's stores. The state-controlled Bezeq will be facing additional competition when the government licenses two new operators of international phone services.

BY GENE G. MARCIAL

SUMNER IS PLAYING THIS SLOT

If you pay attention to corporate insider buying, watch WMS Industries (WMS), the leading maker of pinball machines. Several officers, including Neil Nicastro, president and co-CEO, have been buying shares, now at 16 after climbing above 20 in September. Rumors say Viacom Chairman Sumner Redstone, who already owns nearly 25% of WMS, is increasing his stake.

What's going on? Two things: slot machines and fresh takeover talk.

WMS, also big in video-arcade games and video-lottery-terminal systems, is going into slot machines with a model analysts insist is more entertaining and profitable than existing one-armed bandits. International Game Technology now dominates the business, but Nicastro reckons WMS will prevail. "We go into a business only when we're sure we will become No. 1 in it," he says.

WMS expects approval soon to market its machine in Nevada and other states that permit gambling. Some analysts say the device, now being tested in Missouri and Wisconsin, "outperforms and outearns" other slots. The

HEADING FOR A JACKPOT?



new machine has digitized technology that produces superior music and sound effects. And apart from jackpot winnings, the machine offers several other plays that produce big payoffs.

"It's not just a jackpot machine but an entertainment system as well," says Leo Rishty, editor of *Unique Situations*, a New York market-advisory publication. In addition, Rishty is high on WMS because of Redstone's avid interest. He thinks Redstone wants to add WMS to his Viacom-Paramount-

Blockbuster stable to strengthen his hold in entertainment and gaming.

This is partly why Nicastro and others have been buying, Rishty believes. Nicastro and his father, Louis Nicastro, chairman and co-CEO, own a combined 6% stake. "The Nicastro's know that once WMS gets into slot machines, earnings will explode and the stock will run up again," says Rishty. So his estimates are higher than the Street's: He sees WMS making \$1.70 a share in 1995 and \$2.25 to \$2.50 in 1996.

Predicting a Redstone takeover is investment adviser Charles LaLoggia, who says WMS is "extremely undervalued based on the company's assets." His buyout price: 40 to 50 a share.

A DRUG THAT COULD GET ELAN HOPPING

For a pharmaceutical company whose marketing partners include some biggies, Ireland's Elan (ELN) doesn't get much respect on the Street. At 34, the stock is near its 52-week low. But don't be fooled. "Elan is one of the best bets in health care because of its scope and diversity," says money manager Graham Tanaka. He has been snapping up shares since January, when Elan slipped from its high of 47.

Elan specializes in delivery systems that let certain drugs be administered less frequently, with fewer side effects, and in some cases at reduced dosage. What's more, in a few months Elan may gain a new product to enhance growth.

Elan's strategy, which has produced revenue and earnings growth of 30% a year, is to develop and market products through such majors as American Cyanamid and Marion Merrell Dow. Over the past five years, Elan's growth has come from royalty and manufacturing income, mainly from these two companies. Combined, they accounted for 70% of royalty income in 1994.

Some analysts worry such growth can't be sustained: Certain products, such as Cardizem CD and Verelan, are maturing. But Elan has other products that could boost growth, says analyst Richard Vietor of Merrill Lynch.

He thinks a critical new source of earnings is Naprelan, whose approval by the Food & Drug Administration is believed imminent. Naprelan is a once-a-day version of Syntex' twice-daily Naprosyn, still among the most-prescribed treatments for arthritis. Vietor says Naprelan alone could yield 20%

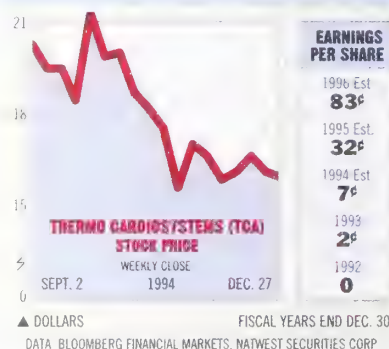
of Elan's earnings. A successful introduction of Naprelan in the U.S. could add 25¢ to 30¢ a share to Elan's net. In 1996, calculates Vietor. He sees Elan making \$2.55 in 1996, up from an estimated \$1.90 in 1995 and \$1.43 in 1994.

DISCOUNTING A CAUTIONARY TALE

When Thermo Cardiosystems (TCA) won FDA approval in October for its HeartMate, which assists pumping the shares got a jolt—and shot to high of 21. They've backed off since, to 16, after an unfavorable tale made the rounds: that HeartMate faces tougher competition than previously thought.

Still, some are scooping up shares. "We think the story is exaggerated

INVESTORS MAY TAKE HEART



and the stock is suffering from a misperception," says Dan Veru, president of New York's Awad & Associates Asset Management. "The stock could double in 12 to 18 months." Marie Conway of NatWest Securities agrees. "This alleged threat is more smoke than substance," she says. Conway believes rivals have "considerable disadvantages."

She calls HeartMate "the most viable" product for congestive heart failure where a transplant is not appropriate or not available. The device can do the pumping of the left ventricle. Other makers of cardiac-support systems include Medtronic and Abiomed.

"We think the market is grossly underestimating Thermo's long-term revenue and earnings potential," says Conway. The company, she says, is "on the cusp of double-digit annual revenue and earnings growth that won't peak for at least a decade." She figures Thermo, 55% owned by Thermedics, will earn 32¢ a share in 1995, 83¢ in 1996, and \$1.52 in 1997, up from an estimated 7¢ in 1994.

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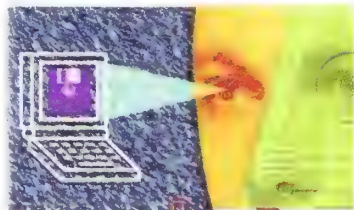
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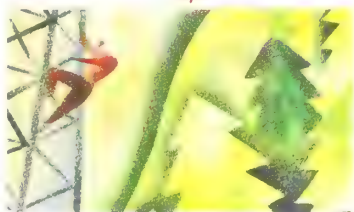
MANUFACTURING

62



HIGH TECHNOLOGY

74



NATURAL RESOURCES

80



SERVICES

84



FINANCE

92

A h, 1994. A year of turmoil from Wall Street to Capitol Hill. The worst bond market in six decades. A battered dollar. An unpopular President. The Orange County bankruptcy. Yet the U.S. economy still managed to put on its best performance in at least six years. Household spending increased. Hiring picked up. Incomes grew. The nation's gross domestic product rose at an estimated 4% annual rate, and a wide range of industries, from autos to computers, enjoyed booming sales.

There's the rub. To forestall a 1970s-style surge in prices, the Federal Reserve raised short-term interest rates six times last year in an effort to cool down the economy. Most Wall Street economists expect that the Fed will take short-term rates up from the current 5.5% level to at least 6%—and possibly as high as 7%—during the first half of 1995. Says Allen L. Sinai, chief global economist at Lehman Brothers Inc.: "The Fed is hell-bent on slowing growth down from the excessive 4% pace of 1994. One way or another, the Fed will get its way."

OVERKILL. Could the Fed's preemptive strike against inflation lead to recession this year? The risk of a steep downturn is apparent. Last year's interest-rate rise will exert its maximum braking force on all kinds of economic activity in 1995. If the Fed continues to tighten well into the first half of the year, the cumulative impact of 1994's restraint and this year's rate hikes could tip the economy into recession. Business executives are concerned. Although upbeat about their own company's prospects, 46% of the respondents to a BUSINESS WEEK/

Harris Executive Poll in December (page 60) said the Fed had been too aggressive, vs. 31% in a similar poll taken only six months earlier.

Yet the odds of monetary overkill seem slim. In the poll, 89% of respondents were optimistic about the economy's prospects, and 88% expected to earn higher profits this year. A resurgent world economy will boost U.S. exports in 1995. Strong corporate cash

flow, global competitive pressures, and evolving technologies will keep capital-goods spending healthy. Most important, inflation pressures will remain moderate. The most economists expect that consumer price inflation will jump from last year's 2.7% rate to 3.5% this year. Yet wage pressures are still slight, consumer inflation is running at its lowest rate in three decades, and by almost any measure, the U.S. money supply is growing at an anemic rate—hardly fertile ground for an inflationary outbreak. "Inflation is too low for the

Growth will be slower—but still not shabby—as a resurgent world economy helps spur the U.S. and inflation pressures stay moderate

Fed to put the economy in recession in 1995," says Mark Zandi, economist at Regional Financial Associates Inc.

Taken all together, the U.S. economy should move along at a moderate clip, 2.5% to 3% in 1995. Corporate profits per share as measured by the BUSINESS WEEK Scoreboard, which tracks the performance of 900 publicly traded companies, should rise by 30% vs. 60% in 1994, according to I/B/E/S International Inc. For the larger universe of companies followed by government statisticians, aftertax corporate profits will come in around 7%, compared with 10% last year. Employment will expand at a 2.3% annual rate in 1995 vs. a 2.6% rate in 1994, according to projections by econ-

OUTLOOK

mic consulting firm DRI/Mcaw-Hill. And college graduates should face an improved job market. A Michigan State University survey of 545 businesses, industries, and government agencies projects a 5.9% increase in hiring of the class of 94-95, compared with last year's paltry 1.1% figure.

High interest charges will be a drag on such consumer cyclical industries as retailers and even-ly cars and trucks. Auto sales are expected to reach their high-level since 1986—15.7 million vehicles. Nevertheless, sales will be only 4%, as opposed to last year's 9% gain. Higher rates will open home sales and residential construction, and spending on household durables such as furniture will shrink. "You're going to see more evidence of the summer sector transitioning to slower growth," says Richard A.ickey, chief economist at Pont Co.

RE CAPACITY. By contrast, hefty capital spending plans Corporate America will keep investors reasonably strong for industries in the information-technology and industrial-equipment businesses. With U.S. factories working at around 84% of capacity, more than 25¢ of each business investment dollar is earmarked for growth in productive capacity, vs. 10¢ just two years ago, according to Edward McKelvey, senior economist Goldman, Sachs & Co. Companies are still trying to boost productivity by adding computer, telecommunications equipment, and software. Corporate technology spending is forecast to rise by some 10% this year.

Key to a solid U.S. economy is emerging global prosperity. Growth is becoming synchronized globally with all the

LEADERS

Pent-up demand and productivity gains will help these industries withstand higher rates

AUTOS America's love affair with trucks and an aging fleet should keep Detroit at full throttle

CHEMICALS Demand is exploding, prices are up, and cost-cutting is improving the bottom line

COMPUTERS From multimedia PCs to powerful network servers, the industry is booming

SEMICONDUCTORS Infohighway and multimedia promise new markets

STEEL Surging demand and new efficiency are driving a resurgence of the U.S. steel industry

LAGGARDS

A rapidly changing environment and Fed tightening will make life difficult for these industries

BANKING Higher interest rates and a decline in mortgage lending will cut into profits

DEFENSE Despite promises of more spending, the industry will shrink with no new weapons programs

PHARMACEUTICALS Managed care and a dearth of new blockbuster drugs will hurt

SECURITIES Rising interest rates will depress sales of stocks and stock mutual funds

UTILITIES Though demand is rising, utilities are unable to raise rates as competition intensifies

world's major industrial and developing nations doing better. Improving economies overseas, coupled with a competitive dollar, could accelerate real U.S. export growth by as much as 10% this year, sharply higher than 1994's gain of 7.7%. Says Michael Fradette, national

director of manufacturing consulting at Deloitte & Touche: "After NAFTA and the GATT treaty, there is a sense of openness to other markets and opening up of export opportunities. Exports will keep manufacturing going strong this year."

Exports will drive corporate earnings growth for a broad array of industries, ranging from manufacturers of telecommunications equipment to fast-food chains to investment banking firms. Any company with a world-class brand name and a strong global distribution network should do well. Even the booming U.S. steel industry is looking to expand its exports for the first time in decades.

BIG JOBS. Europe is emerging quickly from its worst recession in the post-World War II era. The recovery has been largely driven by Germany's export-led rebound, and European output is forecast to expand at a real 3.1% annual rate, up from the 2.2% pace in 1994. Last year's pickup, partly stimulated by government programs in France, Spain, and Italy to subsidize new car purchases, has already hiked sales of U.S. autos in Europe. Among Europe's major auto makers, the European subsidiaries of General Motors and Ford are the second- and third-fastest growing, respectively, according to Autofacts International Inc., a West Chester (Pa.) consulting company. Autofacts expects GM's Adam Opel unit to grow 17% over the next two

years and Ford by nearly 13%—growth that should fatten the parent companies' bottom lines.

To be sure, European governments and companies are grappling with the daunting task of boosting their competitiveness in a global economy. Although

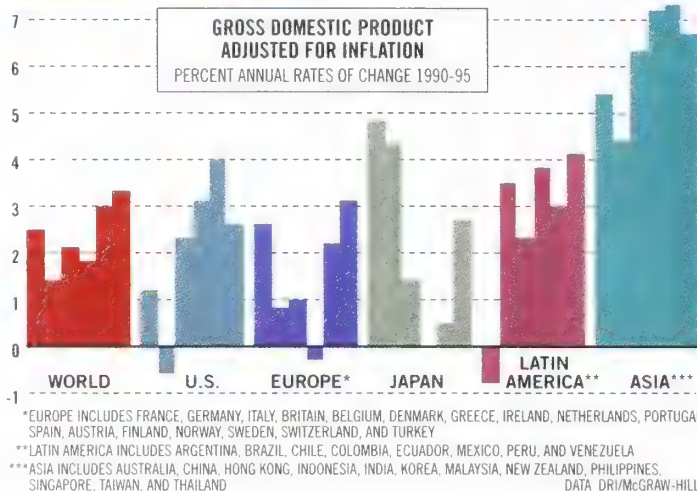
Europe's jobless level stands at 11%, efforts to increase productivity mean that the economic upturn "will not change a large part of the unemployment problem," figures Alexandre Lamfalussy, president of the European Monetary Institute. But Europe's restructuring is a sales opportunity for many U.S. exporters, especially for computer and semiconductor companies. Europe typically absorbs more than 25% of all U.S. capital goods shipped abroad. Among the major European nations, growth in nonresidential capital investment is projected to accelerate by rates ranging from 3.5 percentage points in Britain to 8.5 percentage points in France, according to economists at Salomon Brothers Inc.

In Japan, the world's second-largest economy, growth is expected to improve from an anemic 0.5% last year to 2.7% in 1995. Rising consumer spending is driving the recovery. The improving consumption stems partially from deregulation and partially from a recent \$55 billion income-tax cut. Imports are forecast to grow at double-digit rates, a potential bonanza for American companies in autos, personal computers, telecommunications, medical equipment, prefabricated housing, food, and beverage industries.

American personal computer makers such as Apple, Compaq, Dell, and IBM are enjoying a sales boom, largely thanks to falling import barriers and the growing popularity of American software that runs on their machines. Cut-rate American beer is causing lots of excitement, while U.S. imports of beef, citrus, and juices are more preva-

Economic activity in the world economy should be robust in 1995, a boon to global commerce and international capital flows

WORLDWIDE GROWTH



lent than ever. Even American cars are doing better, albeit from a very tiny base. In the first 11 months of 1994, U.S. auto sales in Japan were up 48.8% from a year earlier.

The world's developing nations are about as big an export market for U.S. companies as the rich industrial countries. The Asian economies should expand at around a 7% annual rate. Despite the uncertainty raised by Mexico's recent peso devaluation, Latin America will grow at more than a 4% pace—the payoff from years of free-market restructurings. The biggest threat to stronger growth would be a repeat of Mexico's devaluation in other Latin American nations, says David Malpass, the director of international economics at Bear, Stearns & Co. in New York.

These days, developing nations are nearly insatiable in their demand for new infrastructure and telecommunications networks. For instance, capital-goods investment in Argentina rose at a

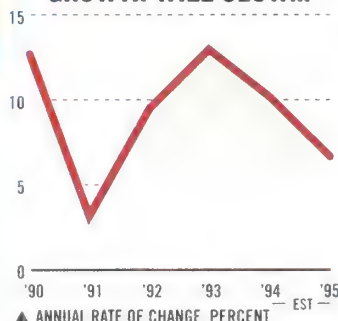
nancial-services industry. European countries plan to sell off \$300 billion worth of assets to private companies over the next decade. Countries in Latin America and Asia are rapidly privatizing their state-run companies, too. With the end of the cold war and the embrace of freer markets by much of the developing world, U.S. investors and corporations are putting billions into overseas economies, says William Sterling, a national economist at Merrill Lynch & Co.

In the U.S., the great uncertainty in 1995 is fiscal policy. Last November's ballot-box revolt makes it likely that there will be tax cuts this year. Typically, tax cuts stimulate economic activity—at least for a while. Yet if Congress fails to slash spending along with taxes, skyrocketing federal budget deficits could send interest rates high. In the BUSINESS WEEK/Harris Executive Poll, 81% favored federal tax cuts only if they were matched by spending

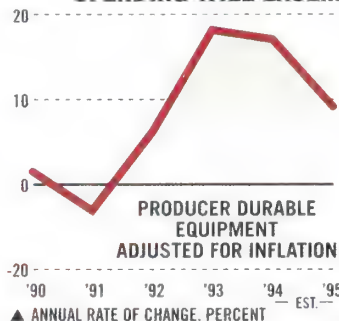
AN ECONOMIC SNAPSHOT

The U.S. economy expanded at a strong 4% annual rate in 1994. The consensus expectation for 1995 is slightly slower growth as the Federal Reserve's hefty interest rate hikes gradually affect economic activity

CORPORATE PROFIT GROWTH WILL SLOW...



...AND INVESTMENT SPENDING WILL EASE...



...AS INFLATION TICKS UP...





EXPORT BOOM

Europe's restructuring is a
es opportunity for U.S.
panies, especially for
se in high technology

s at the same time; only 14%
ked tax cuts even if unmatched
the spending side.

Despite all the focus on Wash-
ton, the economic surprise
ld lie elsewhere. "Productivity
he wild card for 1995," says
hman's Sinai. "The economy
ld still grow faster than 3% and in-
tion stay lower than expected."
The pressures toward disinflation are
verful. Yes, U.S. steel prices are
ging along with rising global dem-
nd, and other commodities and in-
trial materials are showing price in-
ases. Yet in many industries, price
istance is strong at both the whole-
e and retail levels. For instance, the
ntry's 300,000-odd wholesalers and
tributors expect another year of
ong sales and few price increases.
ated competition from other coun-
es with ample labor supplies and ex-
s industrial capacity should keep
ge demands moderate and limit the
lity of most producers to hike prices



STEEL SURGES

U.S. steel prices are rising along with global demand, and 1995 looks like it's going to be a stellar year

in the U.S. And price-cutting is ram-
pant in previously immune sectors of
the economy, such as medical care and
pharmaceuticals.

Even more telling is the seismic
transformation of the U.S. economy.
U.S. companies have made remarkable
strides in boosting productivity by in-
vesting huge sums in high-tech equip-
ment and streamlining operations.
Higher productivity means the economy
can grow faster than expected before
triggering a wage-and-price spiral. In
recent years, the economy's inflation
flashpoint has been pegged at a 6% un-
employment rate. Some economists now
believe that Corporate America's con-
tinual restructurings and reliance on

contingent workers have lowered the
Non-Accelerating Inflation Rate of Un-
employment (NAIRU). The unemploy-
ment rate can drop to at least 5% before
wage pressures prove irresistible.

The recovery is now nearly four
years old, compared with an average of
35 months for all 31 business cycles
since 1854. Many forces affect the du-
ration of any business cycle, but the
most important in a modern economy
is the Fed's war on inflation. If it turns
out that rising prosperity doesn't lead
to higher inflation, the expansion has a
long way to go.

By Christopher Farrell in New York

Introduction continues on page 58

INTEREST RATES CLIMB A BIT...



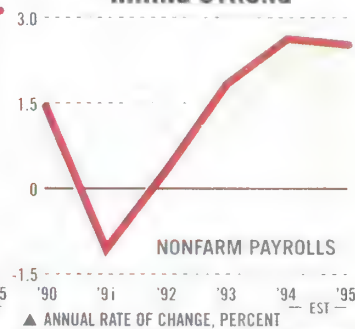
...AND THE HOUSING MARKET WEAKENS...



...BUT EXPORTS WILL STRENGTHEN...



...AND HELP KEEP HIRING STRONG



DATA: DOW/JEWELL, BUSINESS WEEK 1995 ESTIMATE

A SMALLER GOVERNMENT WON'T HURT THE RECOVERY

Washington has caught the downsizing fever from America's corporations, and both political parties are happily getting in on the act.

The Democrats' master plan, the National Performance Review, aims to cut 272,000 federal jobs by 1999. The Clinton White House is also pondering ways to slash agencies, such as the Small Business Administration. Meanwhile, House Republicans, who have dumped three committees and trimmed all panels' staffs by a third, may try to privatize such functions as air traffic control.

IN THE TANK? Listening to all the rhetoric, it almost sounds as if Karl Marx might have been right after all when he predicted that the state would wither away. That may sound appealing to the antigovernment crowd. But what about the dampening effect on the U.S. economy of a smaller government and a balanced budget by 2002, as envisioned by Republicans? After all, the deficit has been providing roughly \$200 billion a year in Keynesian stimulus for a decade. With the federal government accounting for roughly 22% of gross domestic product, wouldn't such strong fiscal medicine tank the economy?

Not to worry. The economy could weather deep spending cuts—so long as they take effect gradually. Seven years would do nicely, government economists say. For one thing, the politicians will focus on attacking just the “structural” deficit, which is driven by policy decisions; the “cyclical” deficit, which provides automatic economic stimulus in the form of higher unemployment benefits and food stamps during recessions, will be largely unaffected.

It's also noteworthy that the annual deficit reductions required to balance the budget in seven years would produce about the same drag on the economy as the deficit cuts Congress passed in 1993. The Congressional Budget Office (CBO) esti-

mates that a seven-year balanced-budget plan would trim the federal share of GDP by four-tenths of a percentage point a year. That's precisely how much federal spending is expected to fall from fiscal year 1993 to 1995. And obviously, the economy hasn't suffered.

Over time, fiscal virtue becomes rewarding. The longer the deficit declines, the easier it is to make further cuts, the General Accounting Office concludes in a new report. The GAO, which examined the effect of deficit reduction in six countries during the 1980s and 1990s, notes that what had once been “a vicious

Mexico. That country's debt fell from 81% of GDP in 1986 to 29% in 1992, while interest costs fell from 50% of total spending in 1987 to 19% in 1992. The net result: one of the best balance sheets among the 24-nation Organization for Economic Cooperation & Development.

LINGERING ILLS. That's not to say that cutting the U.S. deficit won't hurt certain industries or the so-called Gunbelt—an arc that runs through Alaska, Seattle, Silicon Valley, Southern California, the Southwest, and into Florida before turning up the East Coast to Boston. California's lingering ills are testament to

the fact that the state gets 20¢ of every Pentagon procurement dollar. Such spending has been cut drastically, to \$55 billion this year from a 1986 peak of \$120 billion, measured in today's dollars. But according to CBO estimates, California and other defense-dependent states such as Hawaii, Mississippi, and Virginia have already suffered through the worst. In the six top defense industries—ordnance, aircraft shipbuilding, missiles,

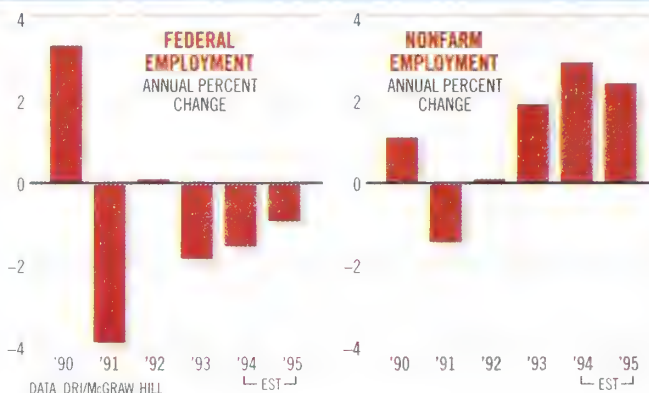
tanks, and search and navigation equipment—employment has fallen 37% since 1986, to 913,000. Further large declines aren't anticipated.

And despite the fact that the federal government may be shrinking, state and local governments aren't. While federal civilian employment has dropped 80,000 since the start of the Clinton Administration, to 2.9 million last August, state and local hirings more than made up for the loss: Total civilian public employment rose 28,000, to 19 million.

Far from hurting the economy, as some feared, President Clinton's \$430 billion, five-year deficit cut enacted in '93 appears to have helped move the economy into the virtuous circle. But with Congress and Clinton catching a new tax-cut bug, don't worry about the feds overdoing the austerity bit anytime soon.

*By Paul Magnusson
in Washington*

THE FEDERAL GOVERNMENT SHRINKS



circle” of rising deficits, debt, and interest costs became a “virtuous circle” of falling deficits and interest costs. The worst case, Mexico, suffered deficits of 16% of GDP in 1982 and 1986—far higher than the U.S. peak of 6.3% of GDP in fiscal 1983. The other countries—Japan, Australia, Britain, Germany, and Canada—had deficits comparable to or slightly larger than the current U.S. deficit. All but Canada managed to turn things around, and none experienced catastrophic economic effects. Just the opposite situation occurred in

*Gradual moves to
cut the deficit seem
to have created a
“virtuous circle”*

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THE TOP BRASS IS GUNG-HO FOR '95

First, some questions about the economy.

Overall, how would you characterize your outlook for the U.S. economy in the next 12 months—would you say you are very optimistic, somewhat optimistic, somewhat pessimistic, or very pessimistic?

	12/94	6/94	12/93
Very optimistic	13	8	3
Somewhat optimistic	76	82	80
Somewhat pessimistic	11	9	16
Very pessimistic	0	1	1
Not sure	0	0	0

GDP GROWTH: SLOWING DOWN

Compared with the last 12 months, do you think the rate of growth of the gross domestic product will go up, go down, or stay the same over the next 12 months?

	12/94	6/94	12/93		12/94	6/94	12/93
Go up	38	44	25	Stay the same	36	38	65
Go down	26	18	9	Not sure	0	0	1

SLIGHTLY SPOOKED BY INFLATION

Compared with the last 12 months, do you think the rate of inflation, based on the CPI, will go up, go down, or stay the same over the next 12 months?

	12/94	6/94	12/93		12/94	6/94	12/93
Go up	53	50	40	Stay the same	40	47	55
Go down	6	3	5	Not sure	1	0	0

TREASURIES: NORTHWARD, NO!

Compared with where it is right now, do you think the 30-year Treasury rate will go up, go down, or stay the same over the next 12 months?

	12/94	6/94	12/93		12/94	6/94	12/93
Go up	57	52	67	Stay the same	24	26	27
Go down	18	18	5	Not sure	1	4	1

LESS SANGUINE ABOUT UNEMPLOYMENT

Compared with the last 12 months, do you think the unemployment rate will go up, go down, or stay the same over the next 12 months?

	12/94	6/94	12/93		12/94	6/94	12/93
Go up	17	13	21	Stay the same	50	44	44
Go down	33	43	34	Not sure	0	0	1

FROM SALES TO R&D, AN UPWARD SPIRAL

And now some questions about your expectations for your company over the next 12 months. Please give your best estimate.

Do you think each of the following will increase or decrease between now and December, 1995?

	INCREASE	DECREASE	SAME	NOT SURE
Sales	91	4	4	1
Full-time employees	47	29	24	0
Investment in plant and equipment	71	13	13	3
Typical prices of standard products or services	63	14	22	1

INCREASE DECREASE SAME NOT SURE

Exports	54	2	13	31
Wages and salary rates	88	2	10	0
Health-care costs per employee	64	16	18	2
Investment in research & development	54	11	25	10

A VERY GOOD YEAR GONE BY . . .

Did your company make a profit in 1994 or not?	12/94
Yes, made a profit	97
No, did not	3
Not sure	0

AND HIGH EXPECTATIONS FOR THE NEXT

(If yes), do you think your profits will increase or decrease in 1995 compared with 1994 profits?

	12/94
Increase	88
Same	3
Decrease	6
Not sure	3

NEWT GINGRICH, PLEASE READ CAREFULLY

The new Republican majority in Congress is proposing billions of dollars in tax cuts that it says can be enacted without increasing the federal deficit. Do you:

	12/94
Favor major tax cuts even if not matched by spending cuts at the same time	14
or	
Favor major tax cuts only if matched by spending cuts at the same time	81
or	
Oppose major tax cuts	4
Not sure	1

FEW RAVES FOR GREENSPAN

How would you rate the job Alan Greenspan and the Federal Reserve are doing—excellent, pretty good, only fair, or poor?

	12/94	6/94
Excellent	16	16
Pretty good	50	58
Only fair	29	24
Poor	5	2
Not sure	0	0

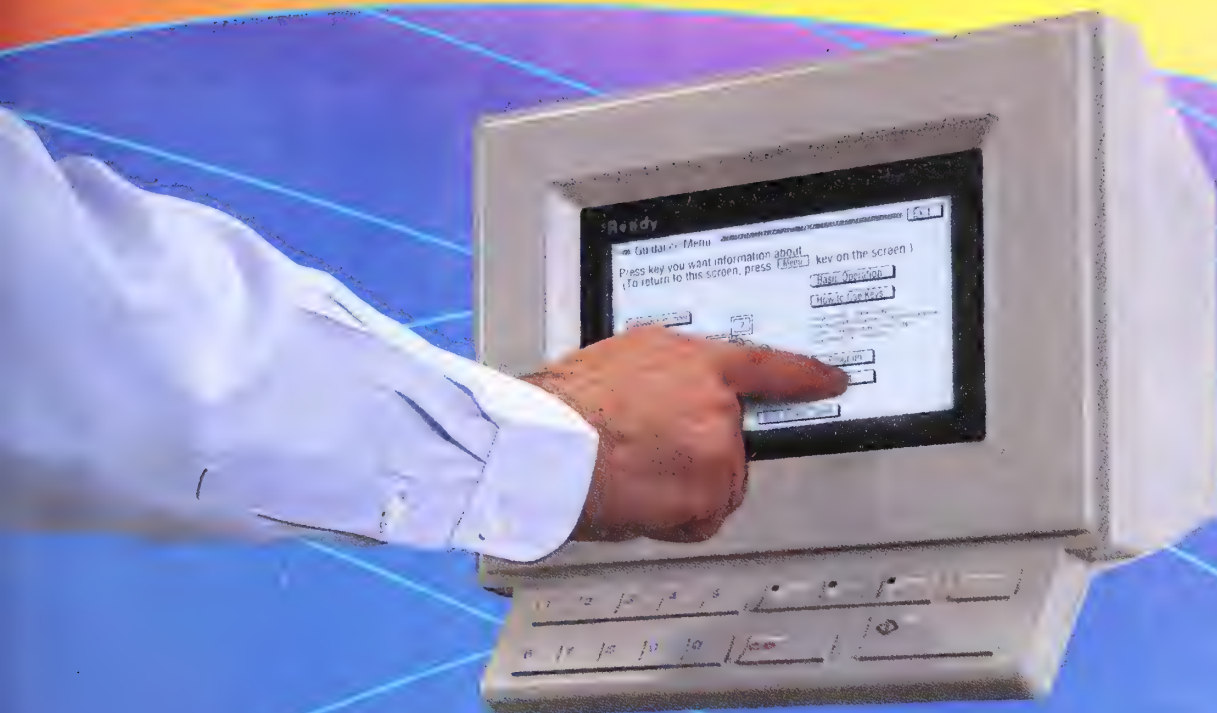
FED RATE HIKE: DWINDLING SUPPORT

As you might know, since the first of the year the Federal Reserve Board has acted to raise interest rates six times. Do you think the Federal Reserve's interest-rate policy has been too aggressive, not aggressive enough, or about right?

	12/94	6/94
Too aggressive	46	31
Not aggressive enough	4	4
About right	51	65
Not sure	0	0

EDITED BY MICHELE GALEN

Survey of 400 senior executives drawn from the BUSINESS WEEK 1000. Interviews were conducted for BUSINESS WEEK Nov. 28-Dec. 9, 1994, by Louis Harris & Associates Inc. Prior polls drawn from the BUSINESS WEEK 1000 were of 401 senior executives conducted on June 1-10, 1994, and of 402 senior executives Dec. 10-20, 1993.



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MANUFACTURING

AUTOS

U.S. carmakers are still in overdrive. The only question marks: Interest rates, costs, and Japan's comeback **PAGE 63**

DEFENSE

The rise in hot spots around the globe means little more than a temporary uptick for contractors **PAGE 64**

MACHINERY

Factories are running at a steamy pace—and manufacturers have the bucks to spend on new equipment **PAGE 65**

STEEL

As foreign markets heat up and Detroit builds more and bigger vehicles, it's happy time at the mills **PAGE 68**

CHEMICALS

With profits bubbling and demand still climbing, even a few price hikes shouldn't spoil the fun **PAGE 69**

FOOD PROCESSING

The cost-cutting and streamlining of the '80s were hard to swallow, but at last they're paying off **PAGE 72**



ILLUSTRATIONS BY MALCOLM TARLOFSKY

BARRELING DOWN A RUGGED ROAD

Detroit has to crank up capacity, keep down costs, fight back rivals—and pray for stable rates

With their factories already running on overdrive, Detroit executives are bullish on 1995. Last year, the market was up a rosy 9%, although the carmakers lost some sales because they couldn't build enough of their longest-selling, high-profit models. In 1995, despite the dampening effect of higher interest rates, U.S. sales should reach their highest level since 1986—about 15.7 million, a 4% gain. And profits should soar. Says Chrysler Corp. Chairman Robert J. Eaton: "1995 will be an outstanding year."

But Detroit clearly remains wary of an eventual downturn. Despite the pressing need to crank out more of their hottest-selling models, the Big Three and their suppliers are hiring sparsely and squeezing more output from existing factories instead of building new plants. Chrysler, for instance, has just added a third crew at the Detroit plant that builds its popular Jeep Grand Cherokees. And Cleveland-based supplier Eaton Corp. has office staff, including the plant manager, working weekends at the assembly line at its engine-valve plant in Kearney, Neb.

GOODIES. The carmakers' other big challenge will be to keep costs in check. Higher prices on such commodities as steel may be inevitable, but to makers are vowing to improve productivity to avoid passing along all of their higher costs to consumers. They'd better. The average car price in the U.S. topped \$20,000 for the first time late 1994, thanks to inflation, increased regulatory requirements, and consumers' preference for bigger vehicles loaded with goodies.

Heading into 1995, Chrysler is the most optimistic, predicting industry sales will near 16 million. The company has \$7.5 billion stashed away against the next downturn, and its pension fund paid up for the first time in 30 years. Analyst David Bradley at J.P. Morgan Securities Inc. pegs Chrysler's 1995 profits at \$4.6 billion on sales of \$57 billion, up 28% from 1994.

Chrysler is betting that its new minivans, due in showrooms this spring, will keep it king of the lucrative segment. Despite quality problems that plagued the Neon subcompact launch and delayed the Cirrus compact sedan last year,

executives vow that customer satisfaction ratings will improve.

Chrysler can't afford another flawed launch. The competition in light trucks is too intense. Ford Motor Co.'s Windstar minivan is gaining share, and the sport-utilities market is burning rubber. This year, hot new entries from General Motors Corp., such as the Chevrolet Blazer compact and the GMC Yukon midsize, plus increased output of Ford's revamped Explorer, will test overall demand for the first time. Says Ford Chairman Alexander J. Trotman: "We'll find out in '95 just how big that market is."

NEW TAURUS. This year, Ford expects to see savings from its global reorganization. And its 1989 acquisition of Jaguar Cars Ltd. is supposed to turn profitable. After being crowned best-selling car three years running, Ford's Taurus will concede the title as its two plants retool for the fall launch of a new model. But Ford expects the stylish new Taurus to regain leadership quickly. Salomon Brothers Inc. analyst John V. Kirnan estimates Ford's

earnings will rise 19%, to \$6.8 billion, on \$119 billion in revenues.

For General Motors, 1995 will test whether CEO John F. Smith Jr.'s two-year-old overhaul is working. Sloppy changeovers to new models crimped GM's 1994 sales and profits. As its factories reach full speed, sales of the products—like the popular new Blazer and Chevy Lumina family sedan—should continue to rebound. Kirnan figures that GM's profits will rise 29%, to \$6.7 billion, on sales this year of \$153 billion.

Meanwhile, Detroit's competition hasn't stalled out. Japanese carmakers, still bedeviled by the strong yen, are cutting costs. And Japanese auto suppliers, already at the top of their class, improved productivity 38% in the past two years, according to Arthur Andersen & Co.

Interest rates remain the industry's biggest question mark for 1995. But consumer confidence remains buoyant, and the average age of cars on the road—eight years—presages plenty of replacement demand. With those factors on its side, Detroit is hoping to spend at least another year running at full throttle.

By Kathleen Kerwin in Detroit

PROGNOSIS '95

MOTOR VEHICLES



POSITIVES

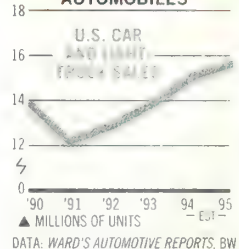
- Consumer confidence is at five-year highs, thanks partly to low unemployment.
- Leasing, which now accounts for 25% of all car sales, is keeping payments affordable.

NEGATIVES

- Rising interest rates will slow domestic sales.
- Higher steel prices and new safety and environmental standards are putting upward pressure on car prices.

SPOTLIGHT

AUTOMOBILES



WASHINGTON WON'T GALLOP TO THE RESCUE

Despite a more pro-military Congress, defense contractors face more shrinkage

PROGNOSIS '95

DEFENSE

AIR, ORDNANCE & SHIPS



POSITIVES

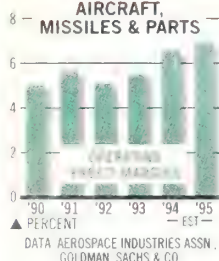
- Cash flow is strong, and the downward spiral in Pentagon budget cuts may have bottomed out.
- The communications sector is growing, and commercial aircraft orders could pick up.

NEGATIVES

- Massive overcapacity means more layoffs and plant closings.
- Backlogs are dwindling, and there are no major, new weapons programs.

SPOTLIGHT

AIRCRAFT, MISSILES & PARTS



Republicans have seized control of Congress. President Clinton has vowed to increase the Pentagon budget by \$25 billion over six years. And after years of painful downsizing, many large contractors were profitable in 1994. Good news for the beleaguered U.S. defense industry? Not a chance. In 1995, a shrinking industry will contract even more as corporations merge, plants close, and more workers lose jobs.

The rise in hot spots around the globe means little more than a temporary uptick in Pentagon spending to handle troop deployments. With no new orders on the horizon, overall military aircraft backlogs, for instance, will continue to dwindle after declining 8% in 1994, to \$79 billion. The Pentagon's procurement budget, moreover, will shrink 13%, to \$55 billion, a 48% drop since 1987.

Despite all its retrenchment, the industry still suffers from massive overcapacity—as high as 50% by many estimates. Even the Pentagon, which on Dec. 9 announced \$7.7 billion in fresh weapons cuts, has conceded that the industry still needs to shrink by at least 20%, according to Paul G. Kaminski, acquisition chief for the Pentagon.

ON THE PROWL. Shipbuilders and submarine makers, such as Tenneco Inc. and General Dynamics Corp., face the toughest fight: Six major companies are almost wholly dependent on military contracts. Yet the Navy has cut its planned fleet size to 300 ships, from 600 in the mid-1980s. Consolidation, already well under way in aircraft, missiles, and electronics, will intensify in 1995. Last year, Lockheed Corp., maker of the F-22 fighter, and Martin Marietta Corp., best known for spy satellites, joined forces to create a \$23 billion defense titan.

Now, in a scramble to beef up dwindling backlogs, a dozen smaller companies are shopping around for partners. B-2 bomber maker Northrop Corp., which just last year snatched up rival Grumman Corp. in a hotly contested \$2.2 billion stock deal, may already be on the prowl for a large electronics company, such as Dallas-based E-Systems Inc. Despite plans to lay off 9,000 workers at the newly merged company, "we're still out there looking" for acqui-

sitions, says Kent Kresa, Northrop Grumman Corp. chairman.

Large conglomerates, meanwhile, which have long enjoyed lucrative defense-contracting sidelines, will take the opportunity to cash out. Analysts say such companies as Texas Instruments, Westinghouse Electric, and Harris are among those likely to put their defense units on the block.

SATELLITE SHOT. At the same time, scores of subcontractors and small suppliers will restructure, merge, or go out of business. Those who remain have been lobbying the Clinton Administration for loan guarantees for arms exports, already a \$13 billion business. But Western European, Russian, and Chinese arm makers are all aggressively marketing their own wares. "Every major country seems to have its own dying defense industry," says Gary Reich, analyst with Prudential Securities.

Commercialization of military technology will likewise offer only spotty relief. Communications businesses have the best shot at success. Raytheon Corp. will attempt to launch commercial satellites from Vandenberg Air Force Base in California, while Hughes Aircraft Co. is planning an expansion of its popular satellite-to-home TV service in Latin America. And Rockwell International Corp. will continue to wean itself from defense dollars: Its recent \$1 billion acquisition of Reliant Electric Co. will boost the company's industrial automation business to \$3.5 billion, reducing military contracts to 18% of revenues from 50% a decade ago.

For aircraft makers such as McDonnell Douglas Corp., which makes the C-17 transport and F-18 fighter jets, there's one bright light on the horizon. For years, the struggling airline industry has delayed purchasing new jets. Now as that industry picks up and new noise-abatement standards kick in, the prospects for new MD-11 orders are improving slightly.

But real industry relief will come when, sooner or later, there are more and bigger wars to fight. An ongoing shakeout of a bloated industry, no matter how lengthy or painful, is far preferable to that.

By Eric Schine in Los Angeles

THE DIN IN HERE IS DEAFENING

Machinery makers will be pressed to keep up with demand from America's booming factories

You say you want to buy a forklift truck? Get in line. How about a machining center to cut some metal parts? You may not find one—en on a dealer's floor. With American factories and mills running at full throttle, the market for general-purpose machinery is booming as it isn't in years.

Can it last? The answer is yes, although the growth expected this year won't match that of early 1994. Orders for some kinds of equipment, such as lift trucks, may be peaking, but machinery makers generally expect another robust year. This is an industry that trails the economy. As manufacturers get up to full speed, they need more equipment. And that's exactly what's happening: U.S. factories are operating at 84% of capacity, their highest rate in more than five years. So naturally, notes Ross J. Centanni, CEO of Gardner Denver Machinery Inc., they're adding [compressed air] needed to run pneumatic tools and other plant equipment. Overall, U.S. machine-tool consumption rose 17% last year, while conveyor shipments closely topped 1993's \$4.2 billion record.

THE STARS? Furthermore, the industry's customers are making more money. "They do have capital dollars now," notes John W. Paxton, chief operating officer of Western Atlas Inc.'s Industrial Automation Group. After years of underinvestment, there's a pent-up demand for machinery. At Mitsubishi Caterpillar Forklift America Inc., Marketing Director Larry Wuench says orders are running 25% above a forecast that was itself revised upward just three months ago. "I don't know if all the planets are lined up, or what," he says. So the joint venture has raised prices about 8% to dampen demand to try to keep up with orders. "My dealers have started to refer to me as 'the business-prevention department,'" jokes Wuench. Best of all, after a decade of brutal restructuring, Industrial America is brimming with confidence. To be sure, there are weak spots, including aerospace and petroleum exploration. But the strong spending is broad-based, from auto makers to steel mills to soft-drink bottlers. And the weak dollar and impressive productivity gains mean U.S. producers are no longer losing ground to foreign rivals.

Even if domestic demand eases—and in some sectors it may—export markets should pick up some of the slack. That includes more than fast-growing Asia and Latin America. Europe, says Cincinnati Milacron Inc. Chairman Daniel J. Meyer, "is a bright spot for Milacron." He sees orders growing by 10% to 25% there this year.

The biggest challenge facing most machinery makers this year is a happy one: How to keep up with demand. For one thing, many companies are short on seasoned engineers. "They used to

be writing us letters, and now we have to go out and look for them," says Roger L. Alderink, engineering vice-president at conveyor maker Alvey Inc.

PUMPS A-PLenty. Suppliers are falling behind, too. "The American manufacturing community is hard-pressed to keep up," says Reginald R. Eklund, president of NACCO Materials Handling Group Inc., which makes Hyster and Yale lift trucks. ITT Corp.'s Fluid Transfer Div. President Dick Labrecque says some foundries that make iron and steel castings for his pumps have increased delivery times from 6 weeks to 26 weeks lately.

After a decade of decline drove many U.S. foundries out of business, a castings shortage now troubles many machinery makers.

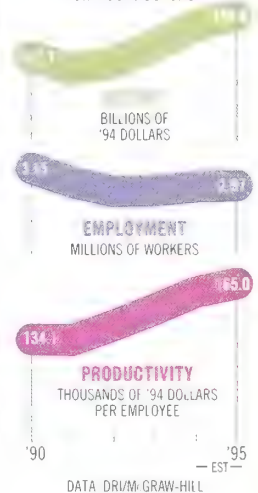
Component and material prices are rising. And machine builders are responding with hikes of their own: Labrecque levied a copper surcharge in September and expects 3.5% to 5% increases early this year. But don't look for a price spiral: Customers have gotten smarter and tougher, so they're not tolerating big price boosts. And in some businesses, such as pumps, there is still worldwide oversupply.

Most important, a disinflationary psychology continues to grip machinery makers. Although they are hiring more people to cope with the demand, they aren't adding substantial new capacity. "The mindset in the early '80s was to get price increases once a quarter," recalls H. Russel Lemcke, a consultant in Seneca Falls, N.Y. "Now we have the same mindset going the other way." Competitive pressures simply won't allow industry executives to abandon their cost-cutting ways.

By Zachary Schiller in Cleveland

PROGNOSIS '95

MACHINERY EXCLUDES COMPUTERS & SEMICONDUCTORS



POSITIVES

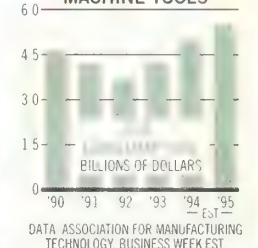
- After years of underinvestment by U.S. manufacturers, there is now pent-up demand for new equipment.
- Profits are up, so U.S. industry has money to spend on machinery.

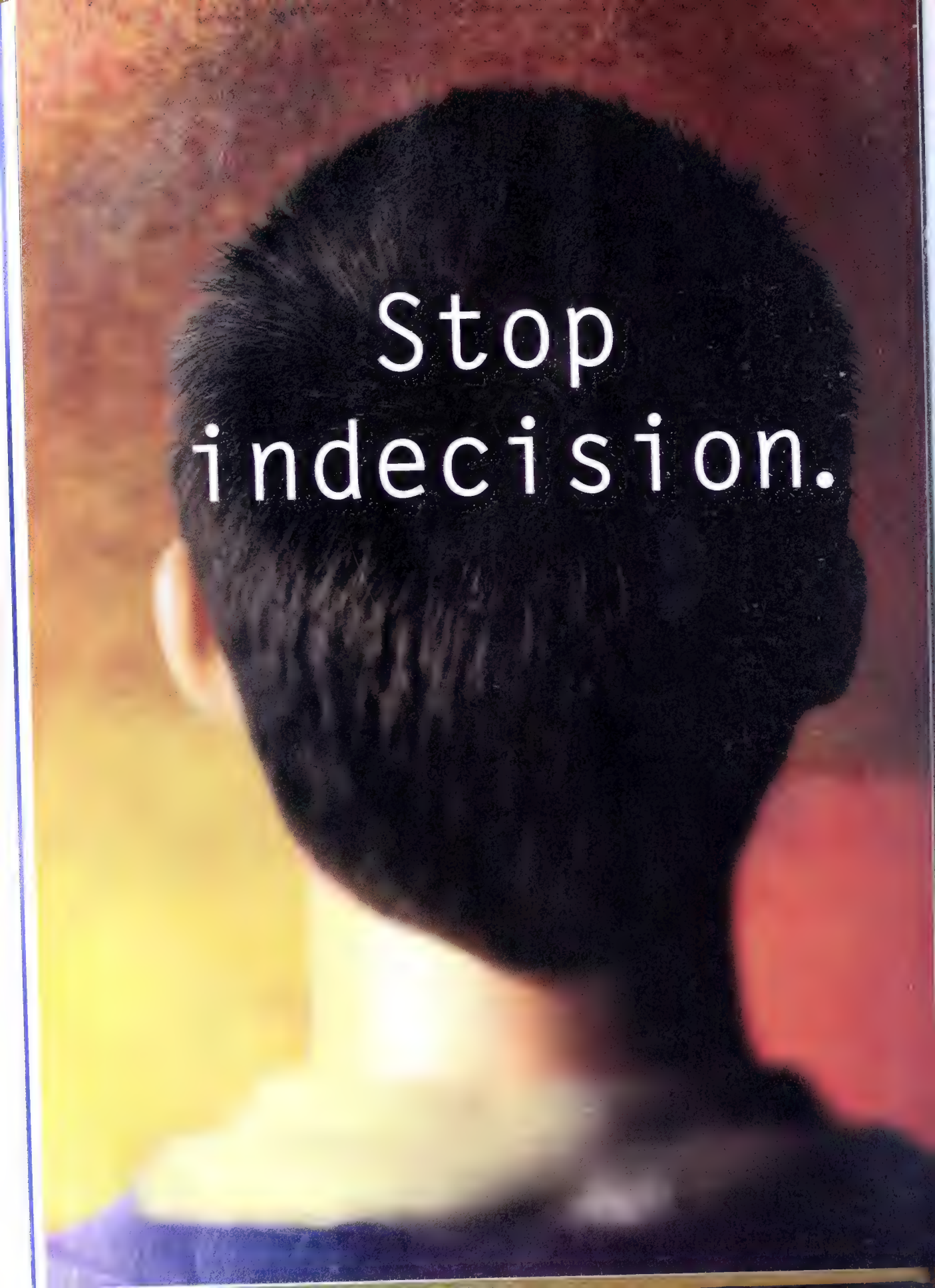
NEGATIVES

- Prices are rising for some materials, while components such as castings are in short supply.
- Finding enough qualified engineers may be a problem.

SPOTLIGHT

MACHINE TOOLS



A photograph of a person with dark, short hair, seen from the back. The person is wearing a light-colored shirt. The background is blurred, showing hints of red and yellow. The text "Stop indecision." is overlaid in white, sans-serif font across the middle of the image.

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CAN ANYTHING DENT THIS INDUSTRY?

The Big Three carmakers and emerging foreign demand have U.S. steel mills on a roll

PROGNOSIS '95

STEEL



POSITIVES

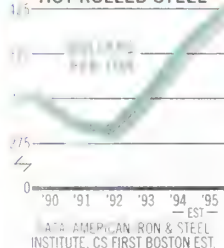
- Strong sales of minivans and other trucks will power demand for flat-rolled steel.
- Robust economic growth in Europe and Asia should keep global steel prices high.

NEGATIVES

- Rising interest rates could dampen the U.S. economy and slow overall demand.
- High prices for steel scrap will continue to pressure margins at minimills.

SPOTLIGHT

HOT-ROLLED STEEL



Rushing to ship before the Great Lakes freeze and price hikes hit, foreign steelmakers sent record cargoes to U.S. ports as 1994 drew to a close. That lifted steel imports to an all-time-high 28 million tons—a 44% jump from 1993. But if this sounds like a dismal replay of the 1980s, when American mills were getting buried under cheap imports, think again. The U.S. economy is relying on imports just to meet booming demand. Led by auto makers, U.S. steel consumption grew 8% in 1994, to 108 million tons. Prices jumped 9%. And the country's appetite shows no sign of slackening. "The markets that are important to us are flashing 'go' signals," says AK Steel Chairman Thomas C. Graham. "We're gearing up to respond to that."

Only an overtightening by the Federal Reserve stands between steelmakers and a stellar 1995. But the coming year should bring a shift: The growth in demand and upward price pressure will come from surging markets in Europe, Latin America, and East Asia, while steel sales flatten in the U.S. This global steel rush is boosting prices from Germany to Brazil. As a result, American Iron & Steel President Andrew G. Sharkey sees imports falling by 3 million to 4 million tons. The more costly foreign steel will bolster U.S. prices. Already, Big Steel has announced a \$30-per-ton price hike. Moreover, analysts expect new longer-term contracts with the auto makers to push prices up by 7% to 10%.

MINIMILL FEVER. The result is near-euphoria among U.S. steelmakers. Buoyed by the cheap dollar and impressive production gains, Big Steel has grappled back into global leadership in price and quality. And integrated companies and entrepreneurs alike are putting up new minimills that will drive down U.S. costs even more. The first, Gallatin Steel, comes on stream this spring in Kentucky with 1.2 million tons of flat-rolled capacity. And LTV, Sumitomo, and British Steel will break ground for a new minimill in April.

Thanks to six-year contracts negotiated in 1993, Big Steel and the United Steelworkers look for labor peace and steady wages. And the USW is playing a key role as independent investors reopen shuttered mills in towns such as Johnstown, Pa., and Sharon, Pa. Workers sacri-

fice wages for equity in these low-cost plants.

Driving the steel boom is Detroit. The Big Three and the foreign transplants raised purchases last year by a blistering 18%. Fully half that growth comes from increased manufacturing of minivans and other light trucks, which consume far more steel than cars.

Steel executives look for auto, construction and appliance markets to withstand higher interest rates in 1995. Integrated companies should

fare better than low-cost minimills, which melt scrap to make steel. Scrap prices follow steel prices up, keeping the minis' margins slim. "Every time you think you've got that sucker under control, scrap goes up by \$20 a ton again," complains Birmingham Steel Corp. Chairman James Todd Jr.

PRICE HIKES. The same global demand that is driving up scrap could turn 1995 into a watershed. Western steelmakers operating at 96% of capacity and Russia's industry

disrepair, Karlis M. Kirsis, director of PaineWebber Inc.'s World Steel Dynamics sees scorching demand outpacing supply. This could send world prices skyrocketing as high as \$600 per metric ton, up from \$420, he says.

Other experts focus more on the dampening impact of interest rates. "I think automobiles have peaked," says Nucor Corp. Chairman Kenneth Iverson, who sees U.S. demand falling in the second half of 1995.

Even so, higher prices should drive up Big Steel's earnings, perhaps doubling from 1994 levels. The companies will clean up their balance sheets. Meanwhile, they'll be pushing into new markets. Steel-frame housing is a growing market, especially in the seismic areas of California. And Inland Steel, Chaparral Steel, and others are forging joint ventures in Mexico, where bridge- and roadbuilding should gobble up steel for years ahead.

Throughout 1995, foreign markets will become the focus for U.S. steelmakers. Their growth will help boost prices in the U.S. And for the first time in decades, American steel companies will be plotting their export strategies, a sure sign of the industry's rebirth.

By Stephen Baker in Pittsburgh

THE CAULDRON IS BRIMMING WITH PROFITS

Burgeoning demand and pared-down, refocused operations should keep the chemical biz bubbling

After running their factories nearly flat out for much of the past year, chemical makers may find themselves hard-pressed to meet all-booming demand in 1995. Executives surveyed by the Chemical Manufacturers Assn. (CMA) expect sales to rise as much as 8% this year, to \$367 billion. And with big price hikes paying off handsomely, profits could rise as much as 15%, to \$3.4 billion. Says Allen J. Lenz, the CMA's economics director: "There's every reason to think 1995 will be a good year for the world economy, and that means it should be a good year for the chemical industry."

Chemical plants are expected to run at over 85% capacity this year, up two percentage points from 1994. And manufacturers will still be hard-pressed to meet the rising demand. For instance, ethylene—a widely used basic chemical whose production was curtailed by flooding in Houston last year—remained in short supply even though those plants are back on line. The result: Ethylene prices soared from 17¢ a pound in the spring to more than 30¢ now.

Some chemical buyers fear that price hikes will continue. DuPont International Inc. in Greenwood, Pa., a \$1 billion-a-year maker of polyurethane foam used in such products as carpet cushions, autos, and mattresses, expects to pay roughly \$5 million a month more for polyols and other raw materials. In turn, the company is charging 8% more for its products.

POSSIBLE PINCH. Still, there are limits to how far the price spiral can go. Higher interest rates could weaken the housing and auto markets, curbing demand for plastics, fibers, and other chemical products. So the smart money is betting that price hikes will moderate, even though that could pinch earnings for some suppliers toward the end. For chemical makers who can't pass on higher ingredient costs, says DuPont Co. Chief Economist Richard A. Stuckey, "profitability could deteriorate."

That's hardly a worry now, though. With big restructuring write-offs behind it, DuPont last year boosted its net income some 59%, to about \$1.65 billion, while hiking sales 5%, to \$39.1 billion, estimates Bear, Stearns & Co. analyst Jeffrey J. Cianci. He figures DuPont this year will

boost its net income 15%, to \$3.06 billion, while lifting sales some 6%, to \$41.4 billion.

Many companies should be aided by savings from years of restructuring. Union Carbide Corp. may save some \$400 million this year, lifting earnings from continuing operations as much as 35%, to \$477 million, after Carbide more than doubled its income last year. The company's sales this year could climb 9%, to \$5.3 billion, Cianci figures.

BACK TO BASICS. Several producers will be helped by a three-year wave of spin-offs that may at last have crested. After selling such non-core businesses as oil exploration and mining in the past few years, W. R. Grace & Co. has its core chemicals businesses down to a more competitive five from over a dozen far-flung units. The result: This year, Grace could boost profits 19%, to \$336 million, on a sales rise of 13%, to \$5.7 billion.

If they stick to their knitting, American chemical companies should stay ahead of foreign competition. So far, worries about global oversupply have proved unfounded as offshore producers in such fast-growing spots as Asia have barely been able to keep up with demand. As a result, the U.S. chemical trade surplus grew 4% last year, topping \$17 billion, says the CMA. It may climb still higher this year. What's fueling it? "We'll have continued very high growth rates for a lot of the less-developed countries," says CMA economist Lenz.

Perhaps the biggest worry for chemical makers is that the good times may blind them to the cyclical industry's inevitable downturn. At larger companies, spending on plants and equipment may rise as much as 18% this year, compared with a 10% hike last year, say executives surveyed by the CMA. Together, large and small companies last year hiked their capital spending some 7.2%, to \$23.4 billion, partly to meet tougher environmental regulations. That figure could rise an additional 13% this year. For now, however, producers have kept other costs in check, shaving employment 1.9% last year, to just over 1 million workers. By avoiding over-expansion now, they'll better weather the eventual bust—whenever it comes.

By Joseph Weber in Philadelphia

PROGNOSIS '95

CHEMICALS EXCLUDES PHARMACEUTICALS



POSITIVES

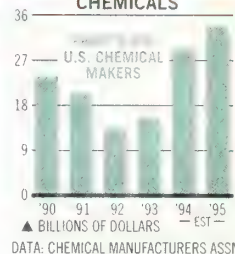
- Recent price hikes are holding, thanks to soaring demand.
- Cost-cutting continues to pay off for most American chemical makers.

NEGATIVES

- Costs for pollution abatement are rising.
- With factories running at 85% of capacity, new spending on plant and equipment could lead to eventual oversupply if the economy slows too quickly.

SPOTLIGHT

CHEMICALS



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THIS NEW RECIPE IS PROVING PRETTY TASTY

After three bitter years, foodmakers find zest in cost-cutting and streamlining

PROGNOSIS '95

FOOD & TOBACCO



POSITIVES

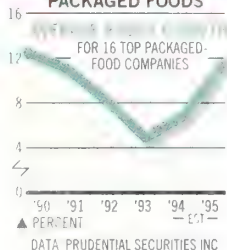
- International opportunities abound as Western Europe and Japan get stronger and developing markets bloom.
- Bumper crops will help agricultural processing companies.

NEGATIVES

- The U.S. market remains stagnant, and consumers won't tolerate price increases.
- Efforts to reduce costly trade promotions could flop.

SPOTLIGHT

PACKAGED FOODS



For U.S. food processors, the heartburn of the past three years is finally giving way to relief. To be sure, the \$282 billion industry still needs to cope with stagnant domestic markets and consumer resistance to price increases. But aggressive efforts to cut costs and increase efficiencies are paying off. While it won't match the Easy Eighties, the last half of the 1990s should bring a modest revival.

Major players will be making overseas expansion a top priority in 1995, targeting Asia, Latin America, and Eastern Europe. Brand-building will return to style, with less spending on promotions to the grocery trade and slower growth of private-label goods. Efforts to improve distribution and cut costs will allow manufacturers to respond more efficiently to their retail customers—and help profit margins.

With better earnings on the horizon, last year's moderate upswing in the stock prices of foodmakers should continue, analysts say. Watch for positive earnings surprises at commodity-dependent companies cashing in on the abundant grain and livestock production of 1994—Tyson Foods, Archer Daniels Midland, ConAgra, and IBP all benefit from cheap supplies. Stock prices also should get a lift as investors shift from cyclical to staples in anticipation of an economic slowdown.

SIMMERING STEWS. Mergers and acquisitions will be the wild card in 1995. Deals involving such household names as Gerber, Borden, and Snapple sparked a flush of takeover fever last year. The stock of Quaker Oats Co. rose and fell as much as 10% in a day on buyout rumors last summer, until the Chicago-based foodmaker agreed to buy Snapple Beverage in November. Wall Street prognosticators muse about H.J. Heinz Co. buying Pet Inc., CPC International merging with Campbell Soup Co., or Unilever PLC picking up any of a half-dozen major U.S. players. Yet the ideal time for a blockbuster deal would have been last June, when stock prices, interest rates, and the dollar were down.

While jumbo mergers could still occur, watch instead for a slew of bite-size transactions in 1995: Borden Inc. selling its Meadow Gold Dairies Inc. to Dean Foods Co., or Quaker Oats unloading its European pet food business to Nestlé.

Why so many smaller sales? Today's sober foodmakers want to build core businesses, focusing on categories where they are No. 1 or No. 2. The hard times of the past three years have led to less risk-taking at home. "I can't imagine that we need to jump into new product categories," says John H. Bryan, chairman of the once acquisitive Sara Lee Corp. The same holds true at ConAgra Inc., an aggressive buyer of companies over the past two decades: It is now getting out of businesses that don't fit, including specialty retailing and direct marketing.

Along with such pruning, brand-building will be highly visible in 1995. It's a crucial year for Kellogg Co. and General Mills Inc., which have sharply cut back coupons and trade promotions on the breakfast cereals in favor of lower everyday prices, consumer promotions, and brand-building campaigns. The risk: Customers used to shopping for bargains might reject the new order.

THE REAL SKINNY. New product introductions, always important, could become a bigger factor as consumer-oriented marketing efforts expand. While diet products such as those from Weight Watchers Food Co. have fallen out of favor, consumers are primed for "healthy" eating. Analysts predict ConAgra's Healthy Choice will continue gaining market share—in part at the expense of strictly diet products. And RJR Nabisco Holding Inc. success with SnackWell's low-fat cookies and crackers will spawn even more imitators. Ralco Holdings CEO Richard A. Pearce foresees a new wave of low-fat cookies, crackers, salty snacks, and sweets that will allow consumers to "have their joy and not pay for it."

Some of the biggest moves of 1995 will be made overseas, as improving foreign economies attract U.S. foodmakers. Companies that have ventured abroad will be testing the waters, and experienced international hands at other companies, meantime, will be seeking growth in new territories such as China: "Anyone who's just sticking a bunch of oars in that water is making a mistake," declares Sara Lee's Bryan. It's a safe bet he won't be the only food executive putting his back into it.

By Greg Burns in Chicago

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HIGH TECHNOLOGY

COMPUTERS

With bigger corporate data processing budgets and a healthy home market, hardware sales stand to soar **PAGE 75**

SOFTWARE

Last year's consolidation trend should keep right on going, and the marketing battle will shift to servers **PAGE 76**

SEMICONDUCTORS

Steadily rising chip content in electronic gear is likely to lead to a third straight year of growth **PAGE 77**

TELECOMMUNICATIONS

Every segment of the industry is seething with possibilities, but players are mostly going haywireless **PAGE 78**

PHARMACEUTICALS

Expiring patents, lots of competition, not much in the pipeline: Drug-makers have a splitting headache **PAGE 79**



ILLUSTRATIONS BY GORDON STUDER

IF IT COMPUTES, IT'S GONNA SELL

The strength in the PC market should spread to servers, workstations—and yes, even mainframes

In an industry where prices can easily tank as much as 40% a year, perhaps the best news in 1995 for computer makers is that corporate processing budgets are going up. After downsizing and putting the brakes on spending much of the 1990s, companies from advertising agencies to local utilities are scrambling to get information systems to find easier and more efficient ways for employees, customers, and suppliers to do business. Corporate technology spending—including computer hardware, telecommunications, and software—will jump 10% in 1995, to \$398.2 billion, according to Gartner Group Inc.

Let the good times roll. With the economy strong, analysts say there is pent-up demand to start automation projects that were put on hold during leaner times. What's more, competitive pressure has intensified in many industries, forcing companies—even as they shrink—to increase automation to improve the quality of their products and services. That's helping to boost worldwide sales of computer hardware to \$142.1 billion in 1995, up from \$123.7 billion in 1993, according to market researcher Dataquest Inc.

EMBRACING THE INTERNET. For computer makers, 1995 is shaping up as the year of the computer server—small, powerful machines from PCs to large parallel-processing computers—that act as traffic cops or big storage bins for information processed by networks of desktop machines. These so-called client-server systems, which let desktop computers share powerful server computers, have become the dominant trend in computing. Corporate spending on PCs is growing 8% a year, but spending on servers is expected to rise 28% this year, according to Morgan Stanley & Co. The main beneficiaries: IBM, Hewlett-Packard, Compaq Computer, and Sun Microsystems. All of these companies have strong offerings in everything from PC servers to mainframe-class machines.

The call for more computer power may even prompt the decline in big iron. For much of the 1990s, sales of these machines slid from 10% to 6% a year. But in 1995, customers will turn to big machines—parallel computers, mainframes, and minicomputers—to support a growing interest

in online databases, access to the Internet, and global E-mail systems. "Mainframes still play a significant role in many enterprises," says International Data Corp. analyst Nancy Stewart. Adds Gartner Group analyst H. Michael Braude: "The stampede to get off the mainframe is abating."

That's good news for IBM. Annex Research estimates that Big Blue—with 80% of the mainframe market—could see a slight 3% bump in 1995 worldwide revenue to \$8.9 billion, up from \$8.6 billion in 1994. That would be the first growth in IBM mainframe revenue since 1990, when that segment of Big Blue's business hit \$16 billion.

All the interest in computer servers doesn't mean the battle for the desktop is over. In 1995, claims Robert G. Pearson, marketing director for workstation supplier Sun Microsystems, there will be a new market emerging for "enterprise desktops." Sun is vying for high-power tasks such as corporate-wide order-entry or inventory-management systems. "The PC is not the answer to every

single form of computing, and it never will be," says Pearson. Meanwhile, workstation makers could benefit if sales of Pentium-based PCs don't take off as fast as originally predicted. Corporate buyers may wait until machines with bug-free Pentiums start shipping in volume. What's more, with Microsoft delaying the rollout of Windows 95 until August, many corporations may postpone buying more powerful machines until then. Overall, according to market researcher International Data Corp., workstation sales will rise 8%, to \$12 billion.

Still, the strongest part of the hardware market is easily the PC. Dataquest estimates that worldwide revenue will soar to an estimated \$93.6 billion in 1995—up from \$73.6 billion in 1993. That makes the PC the single-largest segment of the computer business. And on the home front, PC sales are exploding—accounting for nearly 40% of all hardware purchases. With a healthy home market and bigger corporate data processing budgets, computer makers could be in for a whole new wave of growth next year.

By Ira Sager in New York, with Robert Hof in San Francisco



PROGNOSIS '95

COMPUTERS

INCLUDES OFFICE EQUIPMENT (U.S. ONLY)



POSITIVES

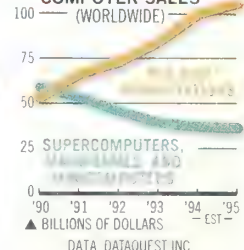
- Sales of computer servers, from PCs to mainframes, are booming.
- Home computers will continue going strong.

NEGATIVES

- Corporate sales of Pentium-based PCs will be slow during the first half of 1995, as companies wait for machines without the defective chip.
- Minicomputer sales will remain flat.

SPOTLIGHT

COMPUTER SALES



ONCE AGAIN, SOFTWARE IS SEETHING

Merger-and-acquisition activity is apt to intensify, and Windows 95 should shake things up

PROGNOSIS '95

SOFTWARE & DATA PROCESSING



POSITIVES

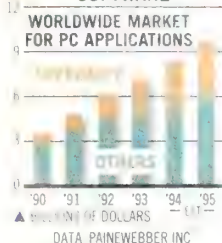
- Strong sales of PCs into homes fuel demand for multimedia CD-ROM titles.
- Online services and the Internet create fresh opportunities.

NEGATIVES

- Microsoft's Windows '95 could be delayed until late 1995, deferring a major upgrade cycle for application makers.
- Last year's price wars in PC software will move to the server market, lowering margins.

SPOTLIGHT

SOFTWARE



That giant sucking sound you heard last year just might have been software companies being swallowed up. Software makers displayed a voracious appetite in 1994, engineering a record \$6.6 billion in mergers and acquisitions, according to Broadview Associates LP, an investment banker. The largest deal—Microsoft Corp.'s pending \$1.5 billion purchase of Intuit Inc.—nearly matched the \$1.6 billion shelled out for 1993's 10 largest deals.

That's just the beginning of a trend that should intensify in 1995. Software companies spent last year bolstering their war chests: Lotus, Microsoft, and Oracle all won board approval to issue more stock that could be used to fund hefty acquisitions. And new players, including cable-TV and telephone companies, are expected to jump into the fray. "Convergence is what's going to drive 1995," says Charles Federman, a managing director at Broadview.

Sure, maturing industries tend to consolidate. But there's more at work here than an orderly evolution. It's becoming clear that in software, bigger is not only better, it's required.

Software companies need look no further than Microsoft for proof. With an estimated \$5.2 billion in revenues for calendar 1994, Microsoft accounts for more than a third of all PC-application sales, including 80% of sales of "suites"—groupings of popular applications. And Microsoft plans to increase spending on research and development by 45%, to more than \$800 million in fiscal 1995. With the desktop pretty much sewn up, much of that investment is going into "enterprise" systems—industry jargon for powerful, behind-the-scenes servers that dish out data to networks of PCs and generally keep businesses humming.

SUITE STRATEGY. Microsoft is making headway: Its Windows NT operating system has started to catch on in the server market, where Unix and Novell Inc.'s NetWare dominate. And the company plans to extend its successful suite strategy into enterprise servers with Back Office, a collection of basic programs—such as database, administration tools, and electronic mail—packaged in a single, low-cost bundle for NT. While Back Office is not expected to be complete for at least another year, it has sent a wake-up call to rivals

such as Oracle Corp. and Sybase Inc., which have enjoyed high-margin profits selling their database products for mainframes and Unix servers. But with demand in Europe and Japan heating up, database companies will still "be printing more clear into 1996," predicts Paul V. Cabbage, an analyst with Dataquest Inc.

Another bright spot for software makers is the consumer market. Some 7 million multimedias equipped PCs were sold to homes last year, fueling the demand for around \$1 billion in CD-ROM software, such as reference and "edutainment" programs. Sales of consumer titles are expected to grow another 25% this year.

BUILT-IN CONNECTION. What should have been the biggest event of 1994—the arrival of Microsoft's Windows update—was a no-show. The company's latest projections are for an August release of the product, called Windows 95, but industry watchers say it could slip further. Even so, more than any upgrade before it, Windows 95 has the potential to radically shake up the software market and precipitate the transition from 16-bit to more powerful 32-bit systems. In one thing, some 20% of the 60 million Windows customers are expected to make the switch in the first 12 months. That, along with new sales by other makers, could bring in a cool \$1.5 billion for Microsoft in the first year.

Windows 95 also foreshadows some of the dramatic changes in store for the software industry. It will come with a built-in connection to Microsoft's Network, an online service that will eventually let customers shop or do their banking electronically and will compete with the likes of America Online and CompuServe.

Online services—and the ubiquitous Internet—are creating fresh chances

for startups and established software companies alike. Some seasoned players, such as Lotus Development Corp. and AT&T, with its Network Note, plan to use private networks to deliver services.

Indeed, as companies rethink their strategies for the coming digital world, the very definition of a software company is changing. By year's end, it may become more and more difficult to tell a software company from a bank or a Bell.

By Amy Cortese in New York



THE I-WAY 'WILL BE PAVED WITH SILICON'

Intel and its rivals will reap plenty of profits as new products and services snap up chips

You can't blame chipmakers for sounding a little cocky. In 1993, they posted their best year since 1988, hiking revenues 29%. In 1994, they blew through a conservative 14% forecast to grow 29% again—to \$100 billion worldwide. This year, while the Semiconductor Industry Assn.'s official forecast mirrors last year's—15%—many chipmakers openly predict a record straight year of 20-plus growth.

They might be right. Although the discovery of a bug in Intel Corp.'s Pentium microprocessor just before the holiday selling season was a public-relations disaster, there's no sign of a slowdown in the overall market for personal computers, the biggest consumer of chips. Indeed, the multimedia boom is sparking robust demand. Telecommunications and consumer electronics—helped by a recovering Japanese economy—also look strong. And the coming Information Superhighway promises huge new markets.

What about rising interest rates? A slowing economy? No problem. "Since 1989, the industry has plowed through every recession and kept growing," says G. Carl Everett Jr., senior vice president in charge of microprocessors at Intel, the world's largest chipmaker.

SLAM-DUNK STAR. Sure, worrywarts can find reasons to fret. Makers of chip-manufacturing gear, such as Applied Materials Inc. and Megatec Corp., report slowing orders. One market watcher, VLSI Research Inc. President G. Dan Hutchinson, even thinks chip sales could drop 5% as the economy slows. Investors are wary, too: Many chip stocks are well below their highs. But for now, danger signals are faint. Despite the Pentium snafu, microprocessors will remain the slam-dunk star. Sales are expected to climb 15%, to \$15.4 billion. Intel, which holds nearly 40% of the business, will see serious competition—mainly 486 chips from Advanced Micro Devices Inc. and Cyrix Corp. Then there are 486 PowerPC chips from the joint venture of IBM, Motorola, and Apple Computer.

Still, once Intel begins shipping bug-free Pentiums in large volumes in February, its sales could soar. Analysts expect a 350% increase, to about 25 million units. Erik N. Jansen of Alex.

Brown & Sons Inc. estimates Intel's cost of replacing the defective chips could run to \$200 million. Even so, he says, "Pentium is unstoppable."

Powerful microprocessors, multimedia graphics programs, and other memory-hogging software will boost demand for DRAMs (dynamic random-access memory chips), a business dominated by Korea and Japan. Dataquest Inc. predicts price battles will hold revenue growth at 12%, to \$25 billion—far off 1994's roaring 56% pace.

VIDEO SPUR. Other chipmakers will benefit from the trend to more powerful microprocessors. Cypress Semiconductor Corp. figures it sells, on average, two dozen high-speed memory and logic chips for every Pentium PC. And demand for digital-signal-processing and data-compression chips, which speed up video and

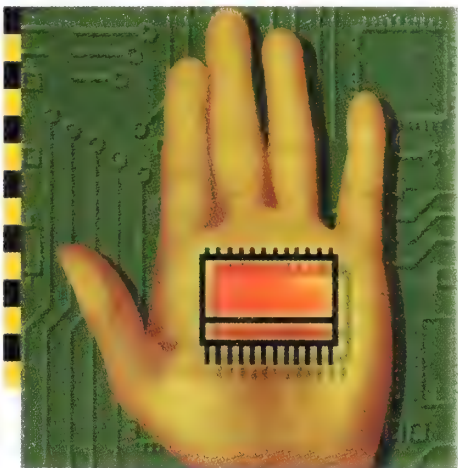
graphics, is red hot. That should boost Texas Instruments, Cirrus Logic, and Europe's SGS-Thomson, plus up-and-comers such as C-Cube Microsystems Inc. and 3Dlabs.

Multimedia chips will gain as phone and cable-TV companies start buying video servers and set-top boxes to deliver movies and interactive games to homes. Intel won't necessarily be inside: LSI Logic Corp. packed microprocessor, graphics, and video-compression circuits onto one chip for Hewlett-Packard Co.'s set-top box. Says TI Vice-Chairman William P. "Pat" Weber: "The Information Highway will be paved with silicon."

After hiking capital spending 35% in 1994, to \$20.3 billion, the U.S. industry will probably throttle back. One exception: Intel will spend more than \$2.5 billion on new wafer-fabrication plants. Japanese chipmakers, who had been coasting on earlier big investments, have resumed heavy spending, mainly for DRAM plants.

Nonetheless, many U.S. chipmakers think their notorious boom-bust cycles are ending. One reason: steadily rising chip content in electronic gear—up from 4% in the 1970s to 10% so far this decade. "I've never seen semiconductor companies so confident in their future," says Frederick L. Zieber, president of Pathfinder Research Inc. Now, if only they can convince shareholders.

By Robert D. Hof in San Francisco



PROGNOSIS '95

SEMICONDUCTORS



POSITIVES

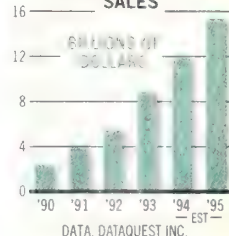
- Booming personal-computer markets drive high demand for microprocessors and memory chips.
- New Information Superhighway markets will ignite sales of multimedia and communications chips.

NEGATIVES

- An uncertain economy could slow rapid growth.
- Profits will suffer if new memory-chip factories cause price drops.

SPOTLIGHT

MICROPROCESSOR SALES



TALK ABOUT DIALING FOR DOLLARS

The telecom industry is growing fast—and its players are salivating over the wireless possibilities

PROGNOSIS '95

TELECOM



POSITIVES

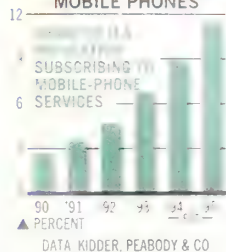
- Long-distance, local, and wireless are growing at record rates.
- Greater competition at the state level is creating new opportunities.

NEGATIVES

- Licenses being auctioned off for new wireless services could end up costing more than expected.
- Regulatory uncertainty is depressing stock prices.

SPOTLIGHT

MOBILE PHONES



It's hard to remember a time when telecommunications meant just phones. These days, new technologies, new rivals, and fewer rules are creating opportunities and markets scarcely dreamed of a few years ago. And business is booming: Long-distance revenues grew 8.4% in 1994 and should rise a further 9% in 1995, according to Merrill Lynch & Co. In local service, the Baby Bells are expected to add new lines at a rate of 3% to 4% in 1995.

And yet stocks of virtually every U.S. phone company have slumped in the past year, with no signs of springing back. Ever since September, when an effort to overhaul the nation's 60-year-old telecommunications rules died in the Senate, a cloud of uncertainty has lingered. Now, the whole industry is nervously waiting to see what—if anything—Congress does this year.

Few observers doubt that cable and long-distance companies will offer local phone service and that the seven regional Baby Bells will be allowed into long distance—someday. But AT&T Chairman Robert Allen doubts it will be this year. "Given the agenda of the Republican Congress—and telecom legislation is not on it—I think that two years from now we still won't have open markets," he says.

GLOBAL REACH. In a world of regulatory status quo, AT&T remains the best-positioned of any telephone company, analysts say. The company is expected to continue to grab market share in the consumer long-distance market in 1995 from MCI and Sprint, as it did in 1994's fourth quarter. As carriers in the industrialized world upgrade their networks to carry video and data and developing nations build their phone systems, AT&T's equipment business, with the most advanced digital technology around, will continue to win multibillion-dollar contracts. Its four-year-old credit phone Universal Card is now the second largest in the U.S. Analysts estimate that AT&T's 1995 earnings will reach \$3.55 a share, compared with around \$3.18 in 1994 and \$2.66 in 1993.

Among the Baby Bells, those that operate in states that have moved furthest toward deregulation or have diversified into nonregulated communications business are best positioned for

1995 no matter what happens in Congress. Analysts favor Bell Atlantic, U S West, and SBC Communications. U S West and Bell Atlantic are moving aggressively into cable, all three have won significant rate relief in their regions, and they all have substantial wireless holdings.

BIDDING WAR. Wireless is the sweet spot of the market. Cellular service, largely unregulated, continues to add subscribers at rates of 50% or more each year, a pace never before seen in telecommunications. All told, estimates Kidder, Peabody & Co. put at some 30 million people, 11.4% of the population, will be subscribing to a cellular service this year. That's more than double the penetration of just three years ago. By the year 2000, the figure should hit 27%, and that's a conservative estimate.

The Federal Communications Commission's ongoing auctions of air space for a low-power wireless network called personal communications services (PCS) is expected to plunk about \$16 billion into federal coffers by the time it is completed at midyear. The first PCS networks—systems that transmit to small wireless phones and cost less to build and use than conventional cellular networks—won't be up and running until the end of 1995. But everyone from Baby Bells to cable companies is forming alliances to bid the auctions.

The favorites are those companies that bid for PCS licenses to fill in geographical gaps in their cellular service to provide a seamless, national network. Once again, that puts AT&T, with its newly purchased McCaw Cellular unit, in the catbird seat, followed by the Bell Atlantic/Nynex/Pacific Telesis/U S West alliance.

But even in wireless, uncertainty rules. No one knows who will win the auctions. And once the winners begin to emerge, new questions arise: How much will it cost to build a network, and when will the returns start rolling in? There are as many answers as there are consultants, and, as one bidder puts it, "PCS consultants are probably the highest-growth business in telecom right now." Proving once again that every segment of telecommunications is a growth industry.

By Catherine Arnst in New York

TAKE TWO ASPIRIN AND CALL IN THE MORNING

Drugmakers have little in the pipeline, lots of expiring patents, and plenty of competition

With Clinton health reforms dead, pharmaceutical CEOs should be popping champagne corks. Instead, they're fretting over thinning margins, dry research pipelines, multi-billion dollar takeovers, and downsizings. "The action has been in Washington, but the action has been in the marketplace," says Douglas G. Mason, president of Ciba-Geigy's U.S. pharmaceuticals business. "Times are tough and getting tougher."

Competition is feverish. Earnings may rise a mere 4.5% in 1995, to \$12.9 billion overall for the biggest U.S. drugmakers, while their sales—plumpped up by acquisitions—rise 13%, to \$14 billion, figures Salomon Brothers Inc. analyst Mariola B. Haggard. Managed care has also tipped the balance of power: The glory days when drugmakers could raise prices at will, reap double-digit earnings gains, and dazzle Wall Street are gone. "You're not going to return to the big growth rates for a long time," says Haggard.

Instead, the industry is in the throes of a consolidation. Dealmakers tallied \$32.8 billion in mergers and acquisitions in 1994, according to KPMG Peat Marwick. Some drugmakers have added distributors, while others are trying to bulk up product lines or lock in promising research. Among the busiest dealmakers are Europeans who want a big stake in the U.S. London-based SmithKline Beecham PLC paid \$5.2 billion for a U.S. drug-rebates company and 3M's Kodak Co.'s over-the-counter Sterling Winthrop Inc. unit.

TECH BLOW. Next, one of the industry's most familiar names—Boehringer-Ingelheim, Warner-Lambert, and Marion Merrell Dow—could be in jeopardy. Although Schering's \$20 billion price tag makes an outright sale unlikely, its healthy product pipeline is a lure. Dow Chemical Co., Marion's major owner, has hired advisers to consider such options as a sale. Warner-Lambert Co.'s recent reorganization—moving drugs, consumer medicines, and medical device divisions into separate operating units—could presage a partial sale.

Biotech companies, reeling from the failures of more than a dozen products in tests, face consolidation, too. Ciba's \$2.1 billion purchase of

49.9% of biotech innovator Chiron Corp. and such deals as Amgen Inc.'s \$260 million purchase of Synergen Inc. will set the pace. And strategic alliances will proliferate. Rhône-Poulenc Rorer Inc. expects to spend \$100 million to fund a consortium of 14 biotech companies and research outfits, avoiding outright purchases.

R&D MINUS. Perhaps the industry's toughest challenge will be to rev up labs at a time when research and development is being squeezed. "There's nothing coming in 1995 where you can say, 'wow, it's a big product,'" says Cowen & Co. drug analyst Robert C. Hodgson. Patents expired on 17 big-selling drugs—with \$8.5 billion in annual sales—in the past two years. Six more—worth \$3.7 billion in annual sales—lose protection by the end of 1996, according to *Med Ad News*. One is Bristol-Myers Squibb Co.'s \$1.5 billion cardiovascular drug, Capoten. A cheap generic would threaten it and Merck & Co.'s \$2 billion me-too drug, Vasotec.

Despite the dearth of new products, the companies will trim R&D costs. Last year, U.S. drugmakers hiked R&D just 9.3%, to \$13.8 billion, the smallest rise in 22 years. And labs are vulnerable. After paying \$5.3 billion for Syntex Corp., Roche Holding Ltd. will cut hundreds of jobs as it moves an R&D lab from New Jersey to Syntex' home in Palo Alto, Calif.

Not everyone is caught short. Pfizer Inc.—bolstered by new drugs and more revenue from its purchase of SmithKline's animal-health business—may see its net income climb 15%, to \$1.45 billion, while sales rise 19.7%, to \$9.8 billion, says analyst Haggard. And Merck's earnings could jump 12.5%, to \$3.38 billion.

Meanwhile, key industry critics have lost power in Washington. "New committee chairmen will have a whole different agenda," says Pfizer chief William C. Steere Jr., who believes the GOP will be less apt to attack the industry's pricing and marketing practices. Still, the new mood in Washington will do nothing to boost R&D or turn back the relentless price-cutting power of managed-care buyers. Those are headaches the industry will be treating this year and beyond.

By Joseph Weber in Philadelphia with Joan O'C. Hamilton in San Francisco



PROGNOSIS '95

PHARMACEUTICALS



POSITIVES

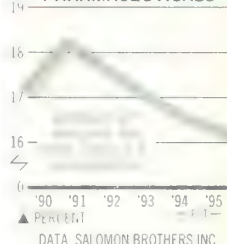
- Cost-cutting will help the drug companies weather newly competitive markets.
- The Republican congressional rout should help the industry on Capitol Hill.

NEGATIVES

- Managed-care buyers will keep pressure on price hikes.
- Generics and the loss of patent protection on some big-selling brands will erode sales growth.

SPOTLIGHT

PHARMACEUTICALS



NATURAL RESOURCES

ENERGY

After a decade of slack demand and painful restructuring, the oil industry is bouncing back. Earnings should gush, thanks to overseas recoveries and cleaner, pricier gas. **PAGE 81**

AGRICULTURE

High-tech gear and glorious weather have helped farmers harvest a bumper crop. This bounty, though, will keep farm prices stagnant even as exports are rising. **PAGE 82**

FOREST PRODUCTS

Papermakers no longer need to plead for orders. Suddenly, prices are skyrocketing and producers running flat out. Lumber, due for a downturn, is still standing tall. **PAGE 83**



ILLUSTRATIONS BY LINDA FRICHTEL

'WE SHOULD HAVE ALL CYLINDERS FIRING'

Upturns abroad, restructuring gains, and cleaner, pricier gasolines should make '95 a winner

For the past decade or so, nearly everything in the oil patch that could go wrong has: Worldwide recession stifled demand, squabbling in OPEC depressed crude prices, and rising environmental regulation and dwindling reserves have forced U.S. oil companies into an extensive worldwide hunt for crude. The result: a massive restructuring that has left 500,000 American oil-industry workers without jobs and shareholders with a cumulative loss of some \$300 billion since 1983, according to McKinsey & Co. But 1995 could be the start of payback time.

Recoveries in Europe and Japan should help boost global demand 1.5 million barrels a day, or 2%, according to the Petroleum Industry Research Foundation Inc. That's the biggest upturn in a decade. Crude prices could jump to around \$9 a barrel, up from \$7.50 in 1994, thanks to rising demand and OPEC's decision in November to extend its current quota through 1995. A strong cyclical recovery in petrochemicals should help, too. And although an initial glut depressed margins in late 1994, refiners eventually could reap a windfall from the introduction of cleaner, higher-priced, reformulated gasolines. "We should have all cylinders firing at the same time in 1995," says analyst Frederick P. Leuffer Jr. of Bear, Stearns & Co. "And you can count on one hand the times that has happened in the last 100 years."

PRO POWER. Overall, earnings should be up sharply in 1995. The top six majors should tally gains of 15%, estimates Merrill Lynch Capital Markets analyst Constantine Fliakos. That turnaround is already under way. Fliakos says earnings improved 10% in the second half of 1994, partly because of petrochemical profits that surged from \$362 million in 1993 to \$2.1 billion last year. Shell Oil Co. is expected to have logged its best second half since 1985. Once considered overleveraged and inefficient, British Petroleum PLC's estimated earnings for the year rose 10%, thanks to cost-cutting and development of gas plays in Colombia, the Gulf of Mexico, and the North Sea.

Not surprisingly, most of the excitement is overseas. With economic growth of 7.2% a year,

"the Pacific region and Asia will be a bigger market than North America by 1997," predicts former OPEC General Secretary Dr. Subroto. That's good news for Mobil Corp., which has 32% of its refining assets in the Far East. A growing number of producers have cut deals with governments eager to supply their energy-starved economies. Some players that have gone all out: Triton Energy Corp. has sold all of its U.S. properties and now operates in 10 foreign countries and is bidding on concessions in 12 others.

There are some wild cards: If Saddam Hussein persuades the U.N. to lift the embargo on Iraqi oil, the annual average price of benchmark West Texas crude may not get much beyond \$18 a barrel. And plentiful supplies and pipeline deregulation will probably hold natural-gas prices below \$2 per thousand cubic feet, despite brisk 3% growth in demand.

Still, oil giants have adapted to lower prices. "With the cash from our restructuring efforts, we're beginning to foresee significant growth opportunities from here on in," says H. Laurance Fuller, chairman of Amoco Corp., which plans to develop the superdeep waters of the Gulf of Mexico with Shell and Exxon Corp. And companies are spending heavily on three-dimensional imaging and other technologies to reduce exploration costs.

Not that restructuring will end. Despite an estimated 16% earnings gain in 1994 and a projected 19% increase in 1995, Royal Dutch/Shell Group is working with McKinsey to overhaul its corporate structure. Texaco Inc. recently sold \$600 million in properties to Apache Corp., and Pennzoil Co. plans to divest \$250 million worth of oil-and-gas holdings this year.

But the focus for 1995 will clearly be on offense, not defense. With free trade on the rise and developing markets thirsty for oil, "we're talking about a growth cycle that's unprecedented in history," says Amoco's Fuller. "Just when [the doomsayers] think they're looking at a sunset for the oil business, they're looking at a sunrise again." Oil executives have been known to see rosiness like that before. But this year they just may be right.

By Peter Burrows in Dallas

PROGNOSIS '95

ENERGY
COAL, CRUDE OIL & GAS,
PETROLEUM REFINING



POSITIVES

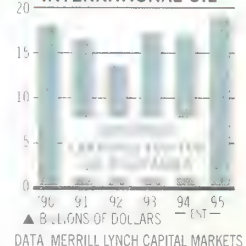
- Rising global demand and higher crude prices should bolster bottom lines.
- Continued restructuring and cyclical upturn in petrochemicals should help energy stocks on Wall Street.

NEGATIVES

- Natural-gas prices could stay low, due to pipeline deregulation.
- Possible lifting of embargo on Iraqi oil could cause midyear dive in oil prices.

SPOTLIGHT

INTERNATIONAL OIL



FULL GRANARIES DON'T MEAN FULL POCKETS

Perfect weather and high-tech methods mean abundant harvests—and lower prices

PROGNOSIS '95

AGRICULTURE



POSITIVES

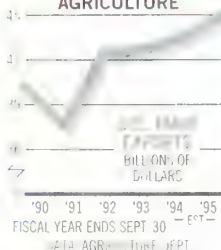
- World demand remains strong. NAFTA and GATT accords will help pump up volumes.
- High-tech equipment and supplies will give U.S. farmers an even bigger edge.

NEGATIVES

- A Republican-controlled Congress is sharpening its budget ax in preparation for the 1995 farm bill.
- A glutted market for hogs and cattle is forcing down prices.

SPOTLIGHT

AGRICULTURE



With a record corn and soybean crop safely in the bin, and vast supplies of livestock fattening on cheap feed, 1995 will be a year of over-abundance for U.S. farmers—and that means low prices. While crop producers should have a decent year even with commodity markets depressed, livestock producers will have a tougher time because they've overbred their herds. Strong export demand will help—especially as the General Agreement on Tariffs & Trade opens new foreign markets. But even so, farm income will remain flat at an estimated \$55 billion in 1995. And it could go lower in future years as a Republican-controlled Congress targets farm-support programs.

To a degree, U.S. farmers will suffer from their own success. The ideal weather of 1994 served to showcase technical advances that will play an increasingly important role this year and beyond. Showing just how efficient they can be when Mother Nature cooperates, U.S. farmers boosted productivity with improved varieties of seed and animal feed, as well as smarter techniques for applying fertilizer and pesticide. And the Farm Belt made big strides in adapting information technology to the barn and field. Even with prices low, 1995 will be another high-tech year for agriculture.

"SwineTRAK." Folks who make a living by the sweat of their brows will harvest their crops with the same satellite navigation systems used by aircraft and ships. Livestock breeders will run software programs such as "SwineTRAK," which determines the ideal genetic match of sow and boar. And on dairy farms, thoroughly modern Bossies will don electronic ID tags that ration their feed and record milk output. The high-tech gear will bring new precision to an enterprise long dependent on guesswork and luck. The upshot: More production from fewer farms. In 1992, the number of U.S. farms slipped below 2 million for the first time since 1850.

That trend is likely to continue in 1995, as the best farmers tap new technology to become even stronger. For the ultimate, look no further than Mansfield, Ill., where farmer Ken Dalenberg drives a combine with two computers and a satel-

lite dish. At harvest time, a global positioning system pinpoints which patch of ground his combine is working while the combine itself keeps track of grain yields. When Dalenberg crunched that data with seed and fertilizer records, he came to tell which plots yield the most and where he needs improvement. Before, Dalenberg made such judgments "by guess and by golly."

With such enhancements—and perfect weather—it's no surprise that production is busting out all over. The 1994-95 corn crop will top 10 billion bushels, up 58% from flood-ravaged 1993-94, the Agriculture Dept. estimates. The soybean crop will top 2.5 billion bushels, and wheat 2.3 billion. Cheaper feed has encouraged livestock producers to expand their herds, and meat supplies are soaring. Unless prices rise substantially, even the most efficient hog producers will have a hard time making money in 1995, analysts say. After substantial gains last year, the USDA projects that beef production will rise 1% in 1995, pork 5%, poultry 5%, and milk production 3%.

The bounty will give U.S. farmers a lot to offer foreign markets, and exports will expand on 1994's gains to a record \$45 billion (chart). GATT should open some markets to U.S. producers. Meantime, trade with Mexico will get a boost from NAFTA, while exports to Taiwan, Korea, and Hong Kong also will expand. China, which tripled its consumption of U.S. farm products in '94 to nearly \$900 million, will pass \$1 billion in '95 with heavy buying of cotton and vegetable oil. U.S. meat exports will rise, led by an estimated 11% increase in poultry shipments.

Other legislation may not be so popular. In addition to sharp cuts in farm-support payout, GOP lawmakers also may seek big reductions in the Conservation Reserve Program. That set aside plan now idles 36.6 million acres, and bringing fields back into production would mean bigger crops and even lower prices. That's good news for seed, fertilizer, and agribusiness companies—but some farmers fear a drastic change. The biggest worry in the Grain Belt this year might not be droughts or floods, but the volatile climate in Washington, D.C.

By Greg Burns in Chicago

THIS PAPER RECOVERY IS NO PULP FICTION

A dramatic turnaround has prices soaring and capacity strained. Even lumber is looking good

As recently as last spring, the paper industry was still mired in its worst slump in decades. Inventories were building up in warehouses around the world, prices had dropped to 50-year lows, and papermakers were begging for orders. But a dramatic turnaround during the summer suddenly reversed the roles. By autumn, it was paper buyers who were desperate. Prices were skyrocketing, and supplies were so tight manufacturers had to allocate production of nearly every grade of paper. "It's almost like a light switch," says Jerry Tatar, vice-president and operating officer at Mead Corp. "We went from having enough orders to having more than we could handle."

After five years of losses or meager earnings, the 19 largest wood and paper companies saw profits jump 108% in 1994. "I call it a rubber-band recovery," says analyst Mark S. Rogers of Prudential Securities Inc. "The industry was stretched so far to the negative side that prices snapped back quickly." Rogers expects a 3% hike in paper prices in 1995 and a 5% rise in profits.

Although the industry's recovery is dramatic, it came later than expected. In 1993, the upturn in the U.S. began pushing up demand for packaging, newsprint, and office paper. But a surge of imports from Europe last winter rattled planned price increases and delayed the U.S. industry's rebound.

AT OUT. Then, last summer, a surprisingly robust recovery in Europe, stirrings of growth in Japan, and continued strength in the rest of Asia tipped the balance. With growth markets in the U.S., Europe, and Asia, demand for paper has finally exceeded supply. "In 1995, it would appear that the three big drivers of the world economy are all trending upward," says John W. Creighton Jr., CEO of Weyerhaeuser Co.

As a result, paper manufacturers are running out: Operating rates are up from 93% a year ago to about 97% today, which is maximum production at most mills. Prices are increasing at the most rapid rate the industry has seen. Market pulp prices rose 87% from their low a year ago, to \$750 per metric ton. Uncoated paper is up 10% since last spring, to nearly \$750 a ton.

Still, manufacturers say prices are just getting back to a level that allows them to recoup the full costs of production. And some say they are phasing in price hikes, so they don't get caught short when power shifts back to buyers in the next downturn. "You don't want the guy madder than hell at you in the next recession," says R. P. Wollenberg, CEO of Longview Fibre Co.

As the cycle turns up for paper, many analysts predict lumber prices will fall as higher interest rates dampen demand for new housing. Yet so far, housing starts have held at an annual rate of about 1.4 million. Plywood is at an all-time high, and lumber prices rallied in late 1994 after a drop during the year. Even if single-family housing starts decline in 1995, multifamily housing starts are increasing smartly. "My view is that next year the market will be softer than this year, but not a major downturn," says George J. Harad, CEO of Boise Cascade Corp.

Despite doomsday warnings, government cut-

backs on timber harvesting in the Northwest

haven't caused a shortage. U.S. softwood lumber consumption has edged down as some builders substituted steel or engineered-

wood products. But imports from Canada have jumped 39% since 1991, and production in the South has risen. Even in the West, mills last year increased production by buying timber from private landowners.

Still, economists say there is a higher floor for lumber prices because of lower federal timber harvests in the Northwest. Prices should trade in the range of \$360 to \$440 per thousand board feet, nearly twice the level of the late 1980s, says Dean Witter Reynolds analyst Evadna Lynn. That's good news for companies that grow most of their own timber, such as Weyerhaeuser, Louisiana-Pacific, and Plum Creek Timber.

Predictions of spectacular earnings growth haven't impressed investors, however. Forest-products stocks have stayed fairly low because of overall worries about interest-rate hikes and slower growth. Wall Street can't seem to believe these paper profits are for real.

By Dori Jones Yang in Seattle

PROGNOSIS '95

FOREST PRODUCTS
PULP, PAPER, LUMBER & PRODUCTS EXCLUDING FURNITURE



POSITIVES

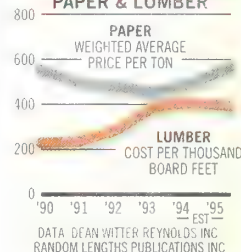
- With the industry no longer suffering from overcapacity, paper prices are expected to continue upward.
- Europe's recovery means less competition from imports.

NEGATIVES

- Higher interest rates may slow housing starts, causing wood prices to fall.
- Used paper prices have risen sharply, increasing raw-material costs for producers.

SPOTLIGHT

PAPER & LUMBER



SERVICES

HEALTH CARE

Market forces are succeeding where Washington failed—in forging a managed-care revolution **PAGE 85**

RETAILING

After last year's surprise pickup, momentum is slowing. Still, apparel sales should dress up bottom lines **PAGE 86**

WHOLESALE

Some will be squeezed out, and price hikes are largely taboo. Even so, the nation's middlemen are smiling **PAGE 87**

TRANSPORTATION

All's fare: Labor and fuel costs are low, business is picking up—but ticket wars keep spoiling the party **PAGE 88**

RESTAURANTS

Hotter competition and a public that won't swallow higher prices may leave eateries a bit hungry **PAGE 89**

UTILITIES

Sparks are flying: With deregulation on the march, the race is on to raise quality and cut costs **PAGE 90**

ENTERTAINMENT

The networks have stabilized—which only makes other media more eager to grab viewers from them **PAGE 91**



ILLUSTRATIONS BY JAMES STEINBERG

SMASHING 'THE BEAST OF MEDICAL INFLATION'

Powerful market-based reforms are trimming private-sector health-care costs

Health-care reform is dead. Long live health-care reform! The sinking of 1994's legislation, while an embarrassment for the Clinton administration, made hardly a ripple in the health-care industry. Instead, powerful currents in the marketplace continued to pull at hospitals, physicians, health-maintenance organizations (HMOs), nursing homes, and suppliers. Employers and insurers are forcing the creation of a new, more cost-effective market. "For health-care companies, it has become a race to see how fast you can squeeze yourself before your buyers squeeze you harder," says analyst Kenneth S. Ramowitz of Sanford C. Bernstein & Co.

The payoff promises to be huge. In the private sector, health-care-cost growth has slowed from double digits in 1990 to just 2.6% in the 12 months ended last June, according to actuary Milliman & Robertson. And competition has led to steep discounting: Inflation-adjusted prices for cardiac-bypass and angioplasty surgeries are actually falling, say health economists HCIA Inc. "The beast of medical inflation has been conquered," says HCIA principal J.D. Kleinke. The glaring exception: Uncle Sam's big health programs, Medicare and Medicaid, which

account for 31% of the nation's health expenses. The Health & Human Services Dept. estimates spending grew 10% in 1994 and will surge another 10% during this year. **EMERGING TREND.** The force behind the changes in the marketplace: managed care. Enrollment in HMOs and preferred-provider organizations has soared. And hard-driving HMOs such as Minnesota-based United HealthCare and Oxford Health Plans in Norwalk, Conn., are holding premium rates below inflation. New entrants—including some Blue Cross plans, which may drop their nonprofit charters to become public companies—will make bidding even tougher. Despite pressure on prices, HMOs maintained margins by striking tougher deals with hospitals, doctors, and suppliers. In 1995, HMOs earnings will climb 15%, Abmowitz predicts. Profits will approach \$3.5 billion, on revenues of more than \$110 billion.

To stay afloat, hospitals will continue to consolidate. In 1994, Columbia/HCA Healthcare swept

up Medical Care America's outpatient surgery centers and took over HealthTrust. The deals will make Columbia/HCA, whose 1992 revenues totaled only \$819 million, the nation's biggest provider, with more than 300 facilities and \$15 billion in revenues. Stiff competition for managed-care contracts has "given hospital CEOs the cover they need to finally run their facilities as businesses," says John F. Hindelong, a principal at Donaldson, Lufkin & Jenrette Securities Corp.

One hard-edged decision: keeping fewer patients in hospital beds. Instead, HMOs and insurers increasingly use nursing homes that offer "subacute care," where patients can recuperate at less cost. Hillhaven Corp., the second-largest nursing-home operator, gets up to \$300 a day for such patients. That's well below a hospital's \$900 charge but a big improvement on Hillhaven's \$88 fee for a geriatric patient. Subacute care will help power earnings growth of 20% or more among the biggest companies.

GLOBAL FOCUS. Medical-equipment suppliers face tougher times. Hospitals banding together in networks share big-ticket equipment, cutting into acquisitions, says Martin E. Zimmerman,

CEO of lease-financier LINC Group Inc. Purchases by U.S. customers are expected to rise only 7%, to \$42 billion. So manufacturers are focusing overseas, where they posted an estimated \$5 billion export surplus in 1994. To escape regulatory bottlenecks on new medical devices in the U.S., some, such as Minneapolis-based Medtronic Inc., are moving product development to Europe.

The industry hopes for—and may get—help from Congress' new GOP majority. Facing severe budget pressures, Congress may make it easier for Medicare to get on the managed-care bandwagon, increasing HMOs' current 7% share of elderly patients. And reforms to make insurance more affordable could increase the market of paying customers. The schemes won't be as grand as Clinton's promise of coverage for all. But they also won't threaten the reforms already well under way in the marketplace.

By Mike McNamee in Washington, with Dori Jones Yang in Seattle and Zachary Schiller in Cleveland



PROGNOSIS '95

HEALTH CARE



POSITIVES

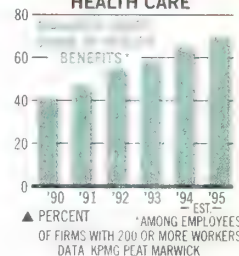
- The search for efficiency will create new opportunities for managed-care and hospital companies.
- Nursing homes will gain as health plans seek the least-expensive setting for treating patients.

NEGATIVES

- Hospital cost-cutting will hurt medical equipment suppliers.
- Washington may limit Medicare's rapid growth.

SPOTLIGHT

HEALTH CARE



STEADY TRAFFIC AT THE MALL

'95 won't quite match '94—but apparel sellers are upbeat, and other retailers even more so

PROGNOSIS '95

RETAILING EXCLUDES EATING & DRINKING PLACES



POSITIVES

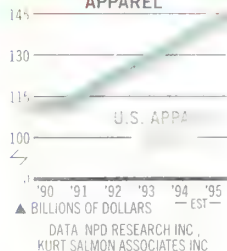
- Consumer confidence is up, and unemployment is at its lowest point in 10 years.
- Apparel sales should improve. Women's apparel prices have fallen, thanks to increased imports and efforts to keep prices low.

NEGATIVES

- Further interest rates hikes could dampen shoppers' enthusiasm.
- A slowdown in housing starts could hurt home furnishings.

SPOTLIGHT

APPAREL



The early 1990s were challenging years for retailers, but the momentum picked up in 1994. Yes, there were some bumps: The department-store industry continued to shrink as Federated Department Stores and R. H. Macy merged, Kmart continued to flounder, and The Limited and Gap showed signs of slowing down. But Sears, Roebuck & Co. staged a remarkable turnaround, the personal-computer business exploded, and sales of men's suits jumped 20% after falling 2.7% in 1993.

So, after all that good news, what will 1995 bring? Carl Steidtmann, chief economist at Management Horizons, predicts that next year will be a decent one for retailers but hardly a stand-out. Steidtmann estimates that retail sales will rise 5% in 1995, vs. an estimated 6.5% jump in 1994. "Raising interest rates increases the cost of mortgages and takes all that refinancing money away from consumers," grumbles Steidtmann. "You're going to see a hit in consumer spending."

GOOD VIBRATIONS. Still, Steidtmann says one of the brightest spots next year will be apparel sales (chart). The price of clothing has fallen, thanks to more imports and the combined efforts of Sears, Wal-Mart, Kmart, and J. C. Penney to bolster their apparel businesses by keeping prices low. Although men's clothing prices crept up 1% in 1994, the price of women's garments dropped 4%, says Marie Beninati of Kurt Salmon Associates. She predicts that apparel sales will increase 5% in 1995, to \$144.5 billion.

The surprise is that despite Steidtmann's less-than-dazzling forecast, retailers are optimistic. Improved consumer confidence, coupled with the lowest unemployment numbers in 10 years, have put shoppers in a good mood. At Sears, apparel is the name of the game. Sears' apparel sales currently make up 28% of the retailer's \$30 billion in merchandise revenues. Since apparel offers fatter margins than hard goods, CEO Arthur C. Martinez wants to increase that ratio to 40%. Wal-Mart CEO David D. Glass also wants to pump up apparel sales. Last year, 27% of Wal-Mart Stores Inc.'s \$55 billion in sales were in "soft goods." The company announced that it, too, wants to increase that ratio.

Not all apparel retailers are prospering. The \$7 billion giant The Limited, same-store sales were in a free-fall in 1994. Gap, a \$3.3 billion chain, had problems, too, with same-store sales just 2%. But the mood at retailers that peddle electronics, furnishings, and jewelry is optimistic. Top executives of Spiegel, Tiffany, Talbots, Pier 1 Imports, Tandy, and Williams-Sonoma are looking forward to 1995. "Right now, I'm smiling," says John V. Roach, CEO of Tandy Corp., the \$5 billion electronics retailer that owns Radio Shack. Tandy's sales increased 25% in 1994, and

Roach expects them to surge another 25% in 1995. William

Chaney, CEO of Tiffany & Co., the \$680 million jewelry retailer, is also cheerful. Tiffany's sales jumped 16% in 1994, and Chaney believes sales could climb 12% to 15% in 1995.

Jewelry sales have been strong at Spiegel Inc., the \$2 billion cataloger, which also owns retail chain and cataloger Eddie Bauer Inc. Spiegel's sales surged 16% in 1994, to \$3.1 billion, and Shea expects them to swell as much as 9% in 1995.

Despite the negative impact that rising interest rates have on housing starts, purveyors of home furnishings feel

optimistic. At Pier 1 Imports Inc., a \$710 million chain, CEO Clark A. Johnson projects that same-store sales will rise 5.5% in 1995, besting 1994's 4% rise. W. Howard Lester, CEO of Williams-Sonoma Inc., which also owns Pottery Barn and Gardener's Eden Inc., is downright ecstatic. Sales of his \$520 million company rose 30% in 1994. Lester expects them to climb 30% in 1995.

Even the folks at Kmart, the lethargic \$34 billion leviathan, are sanguine. Kmart's 1994 results were disappointing: Same-store sales were flat, and the company announced it was closing 110 stores and slashing \$800 million from costs. But Orren F. Knauer, Kmart's director of investor relations, hopes the chain's apparel business, which makes up almost 40% of sales, will drive business in 1995. "Sooner or later, my wife and most other wives will get tired of wearing the same things they've been wearing the last three years," says Knauer. Mrs. Knauer, the retail industry awaits you.

By Laura Zinn in New York

THE MIDDLEMEN STAY ON THE MARCH

Wholesalers and distributors should see plenty of growth along with some consolidation

Perhaps no industry offers a better economic barometer than the nation's middlemen—wholesalers and distributors. And if the chiefs of the 300,000-odd companies that handle everything manufacturers produce—from chemicals and pharmaceuticals to building supplies and packaged food—are correct, 1995 promises another year of strong growth and low inflation.

The middlemen should enjoy a fourth consecutive year of rising sales and profits. Industry revenues are projected to jump 5%, just below the estimated 6% increase, while gross operating profit margins should stretch to 21.2%, up from 20.8%, figures the National Association of Wholesaler-Distributors.

Still, the industry will be vulnerable to this decade's most enduring trends—fierce resistance to price increases and a winnowing of suppliers based on cost and quality. The winners are those able to drive down their costs while providing value-added services, from telemarketing for manufacturers to electronic ordering and purchasing for retailers.

Preparing for the future is proving a painful adjustment for some, however. In December, SuperValu Inc., the nation's second-largest food wholesaler, announced a \$118 million charge against third-quarter earnings, due partly to indigestion after acquiring rival Wetterau Inc. for \$1.1 billion in 1993. The St. Louis company is cutting 4,300 workers, 10% of its workforce, and closing up 30 of its retail stores and several distribution centers.

Chairman Michael W. Wright says the company will benefit from a big investment in technology that helps grocers track inventory. And he thinks some big retailers will reverse the long-standing trend toward in-house distribution and hand the job over to middlemen.

PER PLAYS. In the paper market, United Stationers Inc., the largest distributor of office supplies, saw earnings plummet 26%, to \$15.7 million, on flat sales of \$1.5 billion. One reason was the 1992 purchase of Stationers Distributing. Chairman Joel D. Spungin figures the move is essential in an industry where power disinters, such as Office Depot and OfficeMax, are likely to grab 35% of the market, up from 25% today.

The health-care sector is also being buffeted by change: To control market share for their products, drugmakers have gobbled up drug-distribution and pharmacy-management companies. The consolidation began with Merck Inc.'s late-1993 acquisition of Medco Containment Services Inc., a drug-benefits manager and mail-order distributor, for \$6.6 billion. In 1994, SmithKline Beecham paid \$2.3 billion for benefits manager Diversified Pharmaceutical Services, and Eli Lilly is spending \$4 billion on PCS Health Systems, another managed-care company. The new year will see further consolidation.

The surviving distributors will be bigger and provide more services for their customers. Cardinal Health Inc. spent much of 1994 on a buying spree, nearly doubling in size. Revenues are expected to reach \$7.5 billion this year. Cardinal is providing purchasing and information systems to 3,300 hospitals, doctors' offices, and pharmacies. And as it develops new specialties in areas such as oncology, Cardinal is taking over the telemarketing operations of manufacturers.

EAGLE EYES. In some industries, middlemen are able to push through price hikes. Cleveland's Bearings Inc., a \$936 million components supplier, got a 4%-to-5% price increase late in 1994 on some bearings products—its first boost in three years. Yet customers remain relentless, says Bearings Chairman John C. Dannemiller, rejecting price increases that can't be justified and weeding out shoddy suppliers: "Customers not only want to know whether you are quality-driven but that you can document that you are error-free and provide on-time delivery."

A bellwether for much of the American manufacturing sector, Bearings expects 1995 sales to rise by 10% to 11%, just a shade below 1994's level. Part of that increase, Dannemiller says, will come from new sources. One new income stream is a consortium Dannemiller has put together with two other companies that will provide one-stop shopping and distribution for 90% of customers' maintenance and repair supplies. Distributors, it seems, will search high and low to avoid being squeezed in the middle.

By Richard A. Melcher in Chicago

PROGNOSIS '95

WHOLESALE



DATA: DR/MCGRAW-HILL

POSITIVES

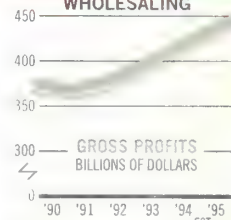
- Strong economy continues to buoy sales and earnings.
- Heavy spending on technology to drive down costs and speed up deliveries gives new life to middlemen.

NEGATIVES

- Customers weed out suppliers, while power retailers bypass middlemen and go directly to manufacturers.
- Distributors will be unable to pass on most price hikes.

SPOTLIGHT

WHOLESALE



DATA: NATIONAL ASSOCIATION OF WHOLESALE-DISTRIBUTORS

AIRLINES CAN UNFASTEN THEIR SAFETY BELTS

Lower fuel prices have boosted profits—but ongoing fare wars make cost control essential

PROGNOSIS '95

TRANSPORTATION



POSITIVES

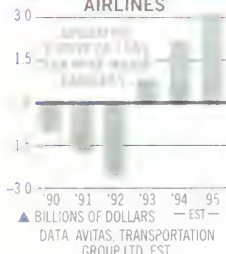
- Profits should climb as carriers cut costs and restrain capacity growth.
- Republican-controlled congress may provide tax relief.

NEGATIVES

- USAir and American may face labor strife.
- A rise in fuel costs would curtail profits.
- Corporate cost-cutting and new communications technologies will mean fewer business travelers.

SPOTLIGHT

AIRLINES



Labor costs and capacity are down. Passenger load factors and profits are up. And, at year-end, not a single major airline was operating under bankruptcy protection. That's the best news the industry has had since 1988. Even better, the good news should keep coming during 1995 as long as the majors continue to cut costs and resist the urge to expand—and the economy doesn't tank.

But don't get carried away. The airline industry's newfound prosperity is fragile. Although 1994 operating profits are projected to hit \$2.2 billion, more than double a year earlier, the nine major carriers are expected to lose \$500 million on a net basis. And revenue has grown a paltry 3.1%. The industry is still climbing out from under years of massive losses. And passenger concerns over flight safety and aircraft maintenance will continue to dog carriers. A close examination of the airlines' 1994 profits reveals that the biggest contributing factor was lower fuel prices, says Renee Shaker, airline analyst with Moody's Investors Service.

Fuel prices in 1994 were 13% below the prior year, but many analysts expect them to rise during 1995. And even if they don't, the airline industry's exemption from the 4.3¢ fuel tax is set to expire in October. That would cut industry profits by \$700 million a year. But some airline executives, including Northwest Airlines Inc. CEO John H. Dasburg, believe the new Republican-controlled Congress will save the industry from more taxes.

ILL WINDS. More fare wars pose another danger to profits. Even low-fare leader Southwest Airlines Co. admits it overdid price-cutting during the fourth quarter in an attempt to hold onto crucial market share in the face of new short-haul competition from such rivals as United Airlines Inc. and Continental Airlines Inc. Southwest's announcement that it would barely turn a fourth-quarter profit torpedoed its stock and caused investors to wonder whether the growing number of Southwest wannabes would cause a permanent deterioration in pricing.

One thing won't change next year: The industry's theme will still be cost control. Delta, American, and USAir are in the midst of drastic cost-re-

duction programs calling for everything from layoffs to wage givebacks to route downsizing.

But even as the major carriers make headway, low-cost carriers are raising the hurdle. Established low-fare airlines such as ValuJet and Reno Air are expanding their reach while new short-haul carriers are coming to such cities as Colorado Springs, Colo., and Pittsburgh.

That's not to diminish the real cost-cutting that did get done during 1994. In July, shareholders approved a \$5 billion employee buyout at United, the nation's largest carrier, that cut labor costs by \$500 million annually. Delta Air Lines Inc. is engaged in a companywide effort to lower its costs to 7.5¢ per available seat-mile in 1997 from their current 9.6¢. More confrontationally, American Airlines Inc. and USAir Inc. are seeking concessions from pilots' unions. Next year, American could find itself with open contracts with all three of its unions.

NICHE SEEKERS. On the bright side, airlines are finally accomplishing what they have talked about for years: shrinking capacity. As loss-plagued carriers cancelled airline orders and abandoned

unprofitable routes, domestic airline capacity declined in 1994, driving load factors higher and boosting profits. By abandoning money-losing routes and adding resources to its profitable hubs, once financially troubled Northwest transformed itself into one of the industry's most profitable players in 1994.

How will airlines boost profits in 1995? After all, traffic was only up about 3% last year, not much to crow about during a recovery. Look for airlines to differentiate themselves through market segmentation, predicts Michael Gelhausen, a managing partner at Andersen Consulting

in Dallas. Picking a niche is important for airlines such as American and United, which have relied heavily on the business traveler. That segment is continuing to shrink as companies cut costs and communication technologies reduce the need to fly. "Even investment bankers don't fly first class anymore," says Moody's Shaker. Maybe not, but if airlines continue to reinvent themselves and trim costs in '95, they just might reach critical altitude—and stay there for a while.

By Susan Chandler in Chicago



BYE-BYE TO FAT TIMES?

Restaurants face higher costs and stingier customers—but a friendly Capitol Hill may help

or the \$290 billion U.S. restaurant industry, the feast of the past few years is giving way to slimmer pickings. Inflation-adjusted industry sales will grow an estimated 2.4%, less than 1994's 2.7% though still a solid gain. Profit margins of major chains will decline to about 5% in 1995, down from 5.2% last year and 5.7% in 1994, according to Technomic Inc., a Chicago consultant. Still, no one is complaining about the news from Washington: An industry that ended 1994 virtually panicked at mandatory employer-funded health insurance extends favorable treatment to a Republican-controlled Congress.

Elsewhere, trouble looms: Rising interest rates and increased competition for desirable sites in key markets drive up the cost of real estate. At the same time, valuing-conscious customers will resist menu price increases. U.S. unemployment statistics, coupled with increased demand for seasoned management, will contribute to a labor shortage likely to force up wages. And if the economy tightens, belt-tightening consumers may start skipping restaurant meals, even as chains expand at 5% in 1995. "Seats are growing faster than fannies," warns David Loeb, restaurant analyst at Chicago Corp.

URGASBORD. Investors are already taking notice. Restaurant stocks were beaten down in 1994, with many finishing the year near their 52-week lows. By Dec. 15, the Piper Jaffray Index of 71 restaurant stocks had fallen 20.8% for the year. Even relatively stable companies suffered: When Brinker International Inc., owner of Outback Steakhouse, told Wall Street in late November that its second-quarter earnings would fall below aggressive estimates, its stock plunged 17%. Other top casual-dining chains, such as Applebee's International, Outback Steakhouse, and Outback Steakhouse, fell with it.

Part of the problem stems from the enormous amount of public offerings in the early 1990s. Since then, in 1991, restaurant companies have raised about \$2.4 billion in public equity, easily surpassing the \$1.7 billion they raised over the previous decade. That boom funded the expansion of some original concepts, and a handful of stocks that

recently dipped into the public till have disappointed. Among the biggest losers: Taco Cabana, Pollo Tropical, Bertucci's, and Fresh Choice.

Now, it's a fight for survival. As chain restaurants continue to open side by side in cities across the nation, the higher costs and stiffer competition will favor bigger operators. Watch for less able chains to add me-too menu items and lean heavily on price specials as same-store sales suffer. The future belongs to well-managed, well-capitalized operators that can lead their categories, whether it's McDonald's Corp. in fast food, Denny's Inc. in midprice family dining, or Brinker in the casual market.

CHEAP EATS. Even big players won't have it easy. At PepsiCo Inc., for instance, Pizza Hut Worldwide will be wrestling with its dine-in business this year. Aggressive expansion of its take-out and delivery outlets has left the Wichita (Kan.) chain well-positioned against Little Caesar Enterprises Inc. and Domino's Pizza Inc. But the higher-margin eat-in business at its 5,100 sit-

down outlets has suffered from neglect. "We have to create a reason for people to come back into our restaurants," says Pizza Hut CEO Allan S. Huston. He's diversifying the menu, offering value meals, and spending up to \$50 million annually to brighten his outlets' worn-out decor, but analysts remain skeptical about a revival. "It's not going to happen," says analyst Allan F. Hickok of Piper Jaffray.

In fast food, bargain pricing will remain prominent. Among burger chains, the majors will continue to stress the 99¢ deals that once gave upstarts such as Checkers Drive-In Restaurants Inc. a price advantage. Checkers, whose stock price has dropped to less than \$3 from \$13 a year earlier, will continue to face stiff competition.

Then, there's that Capitol Hill bright spot: A more business-friendly Congress seems unlikely to impose an employer-mandated health-care plan. Food-service lobbyists plan to take the offensive, trying, for instance, to reverse the recent reduction in business-meal tax deductibility. In 1995, the Beltway bunch may help make up for belt-tightening elsewhere.

By Greg Burns in Chicago

PROGNOSIS '95

RESTAURANTS



POSITIVES

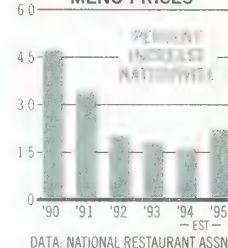
- Industry growth will be solid, especially for big, established chains.
- Restaurants won't be burdened with steep new costs from health-care reform.

NEGATIVES

- As economic growth slows, customers will balk at any increase in menu prices.
- A boom in initial public offerings has encouraged some marginal players to expand too fast.

SPOTLIGHT

MENU PRICES



SUDDENLY, A SUPERCHARGED CLIMATE

Deregulation is coming, so utilities are cutting costs and putting the spark back into services

PROGNOSIS '95

UTILITIES



POSITIVES

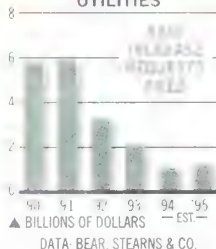
- Demand for electricity is rising about 2% annually, while low fuel prices help keep costs down.
- Full deregulation may be slower than anticipated, giving companies time to adjust.

NEGATIVES

- Price competition could stick utilities with uneconomic, high-cost power plants.
- Big customers are demanding and often getting special rate cuts.

SPOTLIGHT

UTILITIES



Dull. Predictable. Staid. If that's the way you would describe the electric utilities industry, take a closer look. Buffeted by the winds of competition, the utilities industry is one of the fastest-changing segments of the U.S. economy. Big customers are bellowing for lower prices. Regulators are rethinking decades-old monopoly structures. And utilities are scrambling to pare down costs and stimulate torpid cultures. "This is undoubtedly the greatest period of change our industry has ever gone through," says Joseph F. Paquette Jr., chairman and CEO of PECO Energy Co., a large utility based in Philadelphia.

Deregulation has been slowly coming to electricity for 15 years. But the pace of change has picked up markedly in the past two years and could accelerate in 1995. All eyes now are on California, where the Public Utilities Commission (PUC) last April proposed to deregulate almost totally the state's electric power industry by 2002. The most radical suggestion: allow businesses and then residential customers to shop around for electricity service.

BREATHING ROOM. After igniting a lightning storm of controversy, the California PUC postponed its decision and is now expected to make a final ruling in May. Most observers expect it will soften the original plan, perhaps by requiring far more vigorous wholesale competition among power generators as a first step. Once California acts, most other state regulators are likely to study the results before taking action. That could provide a few years of breathing room for hard-pressed utilities.

Even so, most utilities are hustling to prepare for "life after monopoly" by cutting costs and improving service. "Competition is going to come," says Stanley T. Skinner, CEO of Pacific Gas & Electric Co., the largest investor-owned utility. "It's not a question of whether but when." Skinner says he's "hell-bent" on getting ready. In 1995, PG&E plans to cut its costs by \$285 million, partly by slashing 3,000 jobs from its payroll, on top of a 3,000 cut in 1994.

The biggest pressure for change is coming from large energy customers, many of whom are

seeking lower-cost power any way they can get it. Some are threatening to build their own power plants. Others are linking up with local towns to create municipal-owned utilities that can go around the local monopoly utility by bringing power from afar. Then there's Motorola Inc., which is building a big plant in Harvard, Ill., in the territory of high-cost supplier Commonwealth Edison Co. Motorola recently got Com Ed to cut its rates by threatening to build a transmission line to bring in cheaper power from Wisconsin just eight miles away.

To forestall such defections, utilities increasingly are offering steep discounts to keep major customers. One particularly innovative example: Western Resources Inc., based in Topeka, Kan., was concerned that low oil prices could force the closing of many small electric-power oil wells in its territory. So now it's offering operators the option of linking their electricity rates to oil prices.

The newly competitive climate is having impact on utility finances. Unwilling to raise rates for fear of being priced out of the market, utilities filed for a record low \$1.1 billion worth

of rate increases last year, down from \$5.9 billion recently as 1994 figures. Daniel Scotto, analyst at Bear, Stearns & Co. And for all the industry's cost-cutting, Scotto calculates that margins will remain flat, falling in 1995. In

spite demand rising at a healthy 2% annual clip, "the industry's financial profile is as weak as it has been in a decade," he says.

Investors have already taken notice. The Dow Jones utility index dropped 20% in 1994, partly because of rising interest rates but also due to industry uncertainty and cuts in dividends by several utilities.

Although more competition seems inevitable, the precise path to get there remains uncertain. Regulators are still wrestling with huge issues, such as what to do about the billions of dollars worth of high-cost power plants that would be rendered uneconomical if electricity suddenly became a free-for-all. But one thing's for sure: The electricity industry will never be dull again.

By Mark Maremont in Boston
with bureau reports



BATTLE FOR THE COUCH POTATO

The networks are healthy—and everyone from Geffen to Gates wants to compete with them

Imagine the plot. The race is to the swift, with untold riches the prize. The cast includes armies of somber executives, a computer nerd who, a Montana rancher and his actress wife, a mysterious guy from Denver who once prompted a congressional investigation. Sound like a '90s version of the '63 comedy *It's A Mad Mad Mad Mad World*? Hardly. It's the 1995 version of *The Great Race*, and every telephone, computer, and media company in the world wants to want a piece of the business of wiring and delivering programs to America's 94 million homes.

Media companies are staging large-scale tests to see how great an appeal American consumers have for movies, sports, and other services they can order up from their sets. Telephone companies will start airing TV shows for broadcast, two new nationwide television networks will be born, and deals to buy studios and networks will be struck by players positioning themselves to deliver TV into the 21st century.

The Big Three networks, which have been retested for two decades, will be able to own the programming they air later this year. And Baby Bells and cable companies will expand their fight for the rights to deliver programs directly. Freed from so-called Financial Interest Syndication rules, at least one of the Big Three networks will be sold. CBS Inc. owner Laurence A. Tisch wants out, and mogul-without-folio Barry Diller is the most likely buyer. General Electric Co., which wants \$6 billion for NBC Inc. unit, will also finally get a buyer for at least a piece of it.

SOFT OF EYEBALLS. After years of losing viewers to cable and videocassettes, the nets have finally stabilized. Investment bankers Veronis, Suhler & Associates think viewership will plateau at 61% for the next five years after falling most of the past two decades. And in a fractured environment, the larger networks can still deliver impressive numbers of eyeballs for advertisers. "People still want big-event TV," says Fox chairman Chase Carey.

In 1995, network sales for Fox and the Big Three will jump by 5%, to \$11.6 billion—a heady

increase in a nonelection year with no Olympics, says Robert J. Coen, senior vice-president at McCann-Erickson Worldwide. That will mean greater operating earnings for all three, figures Oppenheimer & Co. analyst Jessica J. Reif, with ratings leader ABC earning \$375 million, a 12% gain from 1994 and double its 1993 earnings. Even with hefty losses from its new National Football League contract, Fox will eke out \$10 million or so in earnings, Reif estimates.

MOGUL PATROL. The merging of Hollywood studios and electronic distribution will pick up steam as well. Capital Cities/ABC Inc. is leading the hunt, having already launched joint ventures with video-game company Electronic Arts and the Hollywood team of Steven Spielberg, David Geffen, and Jeffrey Katzenberg. The reason is simple: The battle between competing TV outlets means \$10.5 billion will be spent making TV programs in 1995, according

to Veronis Suhler—a 12% hike from 1993. That has caught the attention of a new cast of Hollywood mogul-wannabes. Eager to deliver video programs over Microsoft's new on-line service, Microsoft Corp. Chairman William H. Gates III is working with Michael Ovitz to line up deals with production companies.

Cable mogul John C. Malone, chief executive of Tele-Communications Inc., isn't likely to stay out of Hollywood for long, either. With cash flow of \$2 billion annually from his nearly 11 million subscribers, he's intent on expanding his core business as well. A \$2.4 billion deal by TCI-controlled InterMedia Partners to buy Viacom Inc.'s 1.2 million subscribers will expand his already massive clout within the industry. He'll want programming to show them and has again started looking to invest in Hollywood studios.

Malone had better move fast. By midyear, the seven Baby Bells will have cemented their own Hollywood relationships. By then, Walt Disney Co. is expected to have formally signed an agreement to provide programming for three of them. Three others allied with agent Ovitz will have already signed their first deals to make TV shows. In all, Hollywood should generate \$18.3 billion in 1995, double its 1988 take. With that much on the line, the plot can only continue to thicken.

By Ronald Grover in Los Angeles

PROGNOSIS '95

ENTERTAINMENT INCLUDES BROADCASTING



POSITIVES

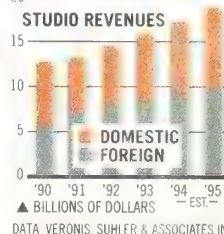
- A stronger economy will boost ad sales for networks and cable.
- New broadcast and telecom-based networks will spur demand for movies and TV shows.

NEGATIVES

- Slower-than-expected demand for interactive services will hamper new marketing trials by cable and telecom.
- A rash of big-budget films threatens Hollywood studio profits.

SPOTLIGHT

HOLLYWOOD



FINANCE

BANKING

Higher rates put a damper on demand in mortgage and consumer banking, thinning out earnings. **PAGE 93**

INSURANCE

A host of environmental claims has rocked the industry, but health-care insurers are reaping hearty profits. **PAGE 94**

SECURITIES

Derivatives debacles and rising rates made for a dreadful year. There's reason to think '95 will be brighter. **PAGE 95**

REAL ESTATE/ CONSTRUCTION

Commercial property is finally back from the dead, but rate hikes may call a halt to housing's climb. **PAGE 98**



ILLUSTRATIONS BY HAYES HENDERSON

A DELICATE BALANCE AT THE BANK

Fewer loans, lower returns—profits won't come as easily this year

Banks have been riding a wave of good fortune for three years now. With low interest rates keeping loan losses falling and profits on investments rising, banks have been rack-up record earnings since 1992. But stellar earnings growth won't come so easy in 1995. Rates are apt to move even higher, the economy is slow, and with excess capacity a continuing problem for the industry, new revenues will be scarcer.

High interest rates are already cramping bankers' style. To begin with, demand for mortgages and other consumer banking products is down. Mortgage lending dropped about 25% in 1994 and will continue to shrink in 1995, according to the Mortgage Bankers Assn. Fierce competition among loan-hungry bankers is also cutting into profits on commercial lending. Says Martin J. Fischek, executive vice-president at a subsidiary of Florida's Barnett Banks and president of Robert Morris Associates, an organization of bank loan and credit officers: "There are going to be a lot of lenders looking for somebody to lend to, and borrowers, with rates high, will be a little less willing to borrow," forcing banks to offer bargain rates.

The losses on investment securities will also eat profits. Rising rates have pushed down prices on bonds and have devastated some banks' portfolios. Banks holding on to bonds with below-market yields can expect subpar investment income until rates come down. Pittsburgh's PNC Financial Services Inc., for one, expects that its interest income in 1995 will be 15% below 1994 levels.

PARING JOBS. Many bankers are taking preemptive measures in anticipation of the more challenging environment. Banks will focus on "expense control, choosing priorities around the world, and managing change caused by technology and communication," says Dennis Weatherhead, the just-retired chairman and CEO of J.P. Morgan & Co.

Already, employment is starting to shrink at some institutions, as Chemical Banking, Chase Manhattan, Fleet Financial, and others announce layoffs or cuts. CS First Boston Group Inc. sees rev-

enues for 35 top banks rising 4.9%, but expenses increasing just 3.2%.

Smart banks aren't just battenning down the hatches, however. They are investing where they'll have a competitive edge. Watch for a pick-up in technology investments, particularly in back offices and consumer banking. A survey by consultants Ernst & Young shows that banks plan to boost technology spending to \$19.8 billion by 1997—21% more than 1994's \$16.4 billion.

Electronic consumer banking will get a lot of attention. A few banks, notably Citibank and NationsBank, already sell or lease "screen phones"—telephones with cathode-ray-tube (CRT) screens attached—in some markets. These phones can

be used for banking business or for ordinary phone calls. In December, Chase introduced a device that customers can plug into an ordinary telephone to do their banking. Other banks will be launching their own home-banking offerings in 1995 and beyond.

As for acquisitions, many banks will focus on small "fill-in" deals that boost their presence in specific fields. One example: the purchase of U.S. Trust Corp.'s securities-processing operations by Chase, which is trying to get economies of scale in that business. Big deals are hardly

dead, though, says Chemical CEO Walter V. Shipley. His bank is the result of a \$2.3 billion megamerger between Chemical and the former Manufacturers Hanover Corp. "Over the long term," he predicts, "more consolidation will take place of the Chemical-Manufacturers variety."

In Washington, banks may find a friendlier environment with the Republicans in control of Congress. Representative Jim Leach (R-Iowa) may introduce a bill to reform the Glass-Steagall Act, the legislation that limits banks' involvement in securities. But potential new restrictions loom. The National Association of Securities Dealers has proposed new rules for the sale of securities in bank lobbies, and the derivatives market could also see new regulations.

The coming year won't be a banner one for most banks. But bankers who invest the capital they amassed in the past few years in well-targeted fields will find reasons to smile.

By Kelley Holland in New York, with Amy Barrett in Washington



PROGNOSIS '95

BANK SERVICES



POSITIVES

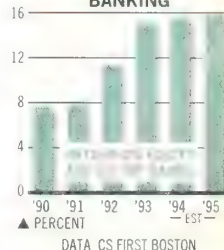
- Banks will cut costs to boost their competitiveness before acquirers do it for them.
- Fill-in acquisitions will help many gain strong positions in well-targeted markets.

NEGATIVES

- High interest rates are cutting into demand for such key products as mortgages and commercial loans.
- Losses on investment securities will reduce many banks' income.

SPOTLIGHT

BANKING



FIELDS OF GREEN—AND DISASTER AREAS

Health care is robust, but environmental claims could drain insurance companies' reserves

PROGNOSIS '95

INSURANCE

BILLIONS OF '94 DOLLARS

EMPLOYMENT
MILLIONS OF WORKERS

PRODUCTIVITY
THOUSANDS OF '94 DOLLARS
PER EMPLOYEE

96 — EST — 95
DATA FROM GRAW-HILL

POSITIVES

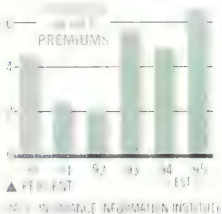
- Premiums for auto and home policies should jump 6.6%, boosting profits.
- Lack of drastic reforms will help health insurers maintain business.

NEGATIVES

- Agents' illegal sales tactics have hurt life insurers.
- Huge environmental cleanup costs dog property-casualty insurers, and disability claims keep rising.

SPOTLIGHT

PROPERTY-CASUALTY INSURERS



How well will insurers perform in 1995? The answer depends on which business they're in. Health insurers, spared reform from Capitol Hill, are still pushing consumers into managed care and reaping robust profits. On the other hand, property and casualty insurers were rocked by the 1994 California earthquake, snowstorms in the Northeast, flooding in the South and West—and a plague of environmental claims. Overall, they paid out \$15 billion for disasters in 1994—their second-worst year in history.

Property insurers still have a hefty \$180 billion in reserves against future losses. But those reserves are coming under increasing strain: Many insurers who sold liability policies in the 1960s and '70s are being asked to fund cleanups of environmental sites. "Environmental claims are the single biggest issue facing the insurance industry," says Dean R. O'Hare, chief executive of Chubb Corp. in Warren, N. J. Indeed, the rating agency A. M. Best Co. predicts that insurers will pay a staggering \$132 billion for environmental and asbestos claims.

That threat is already having an impact. Aetna Life & Casualty Co. added \$200 million to its reserves last year and saw its stock price drop 22%, primarily because of concerns over future environmental claims. And Continental Corp. set aside an extra \$400 million.

BOND TRAP. In 1995, property-casualty insurers will get some short-term help in the form of higher prices. Premiums should increase by 6.6% this year, according to a survey by the Insurance Information Institute. That's up from a 4.9% hike last year—and the increase might help profits recover. Without any large disasters, property and casualty earnings could hit \$15 billion in 1995, up more than 50%.

What could hurt the bottom line, however, is a continued rise in the bond market. Some 62% of the industry's assets are invested in bonds. With a 200-basis-point deterioration in bond portfolios, insurers have lost two years' worth of operating earnings, estimates A. Michael Frinquel, an analyst at Salomon Brothers Inc.

Meanwhile, life insurers were stung last year by revelations that Metropolitan Life Insurance Co. agents were illegally selling policies as retire-

ment plans. The New York company paid more than \$20 million in fines, and it expects to refund \$50 million to policyholders. The brouhaha was partly to blame for a 4% industrywide drop in life-insurance sales last year. "Market conduct may well be the crucial issue for our industry in this decade," says Stephen L. Brown, CEO of John Hancock Mutual Life Insurance Co. "Before, there was a general sense of distrust. Now the public has seen well-defined behaviors that support their feelings about us."

HMO BANDWAGON. Insurers will also struggle with individual disability policies, a \$3 billion market that has been hurt by increasing claims from everything from AIDS-related illnesses to repetitive-stress and back injuries. Provident Life & Accident Insurance Co. of America took a \$4 million charge. And UNUM Life Insurance Co. of America set aside \$125 million for claims and stopped selling the policies in the U.S. "The marketplace is one of fixed prices and increasing costs," says James F. Orr III, UNUM's CEO.

Health insurers are making more money by pushing consumers into managed care. Enrollment in health-maintenance organizations totaled 50 million at yearend, up 12% from 1993, according to the Health Insurance Association. By 1997, managed care will make up 80% of the health insurance market, predicts Allen Maltz, a vice-president at Aetna.

The benefits are clear. Health premiums should rise by 5% in 1995, but overhead will drop by 3%, so managed care realizes economies of scale. That's why the business is attracting entrants. Metropolitan Life and Travelers Corp. combined health-insurance operations into Metropolitan Health. The two hope to compete with CIGNA, Aetna, and Prudential—leaders in managed care.

Last year, the industry got its wish and spared a Washington-led overhaul of the health care system. This time, it's pressing for legislative action: To minimize the growing burden of environmental claims, insurers want the GOP to make Superfund reform—a cap on what insurers would pay out—a top priority. They're likely to win again.

By Chris Roush in Hartford



ON WALL STREET: THIS TOO SHALL PASS

High rates and derivative losses will continue to rankle, but some see a second-half easing-up

Much of the securities industry took it on the chin last year, but there'll be plenty of pain left for 1995. High interest rates, more regulation, and continuing consolidation will squeeze further. "The first half of 1995 will be very difficult, with interest rates as high as they are," says Gordon R. Watson, brokerage group president at Fidelity Investments.

Not all bond traders and investment bankers are crying in their martinis, however. Many Wall Street denizens expect a better second half.

Those at stronger firms see pricing opportunities, from making to issuing stock to foreign governments to adding mutual funds. "1995 will be a better year than 1994," says John L. Steffens, executive vice-president at Merrill Lynch & Co. At some point, rates will turn around and create a better environment for the individual. "Higher rates last year caused big trading losses for securities firms. After three phenomenal years, industry earnings plunged 80% in 1994, just \$1.8 billion before taxes, estimates the Securities Industry Assn. (SIA). In 1995, analysts expect that pretax earnings will edge up to \$3 billion.

Interest rates are expected to rise further in 1995, however, which won't help the equity-commission business. Investors are expected to defect from the stock market to bonds, causing re-trading activity to slow down. While equity mutual funds, according to the Investment Company Institute, attracted a record \$111 billion in the first 10 months of 1994, Lipper Analytic Services estimates that November, 1994, saw an outflow of \$436 million, which could continue into 1995. Higher rates also mean that bond-underwriting activity will stay depressed, since corporations have to pay out more interest.

PROSPECTS. Consolidation and globalization will continue to eliminate jobs. PaineWebber Group Inc.'s takeover of Kidder, Peabody & Co. cost about 2,500 jobs. As U.S. and foreign players scramble to team up to tap global markets, there will be more casualties. If the Glass-Steagall Act is repealed, which may come to pass in 1995, even more jobs will disappear, as regional brokers are bought by regional banks. Industrywide, job losses could exceed 10,000 in 1995.

Intervention from Washington in the lucrative derivatives markets is another approaching storm. Derivatives are a broad category of financial instruments, from futures to structured notes, whose values are "derived" from an underlying security. The bankruptcy of California's Orange County, partly due to investments in especially risky derivatives, has thrust the entire derivatives market under a microscope.

Selling high-margin derivatives has been a bonanza for big Wall Street firms. Some 30% of Merrill Lynch's \$2 billion in net trading revenues in the first nine months of 1994 came from derivatives. If House

Banking Committee Chairman Jim Leach (R-Iowa) succeeds in imposing federal regulations on derivatives, that bonanza could shrink. And activist Securities & Exchange Commission Chairman Arthur Levitt Jr. may fight to oversee the municipal-bond markets, which are currently regulated mainly by the states.

But professional optimists on Wall Street are hardly despairing. Washington may also deliver two huge gifts to the securities industry: a capital-gains tax cut and a restoration of tax deductibility for individual retirement accounts. Merrill's Steffens sees a 60% chance of a capital-gains tax cut and a slightly higher chance for an IRA deduction.

Some firms continue to see big gains by going global. The dominant U.S. investment banks should keep winning lucrative advisory and underwriting assignments around the world. "1994 is not the first year of a long down cycle but an interruption in a favorable trend. We are absolutely convinced that globalization is early in impact," says Richard B. Fisher, chairman of Morgan Stanley & Co., which is hiring overseas.

Other businesses are humming, too. Mergers-and-acquisitions activity exploded in 1994 and is expected to continue at a heady pace in 1995. "Our backlog on M&A is up 40% over last year," says Morgan's Fisher. Merrill Lynch's trust business is growing dramatically, as are research, mortgages, and the privatization of foreign-government properties. But the growth areas will find it tough making up for a lousy year.

By Leah Nathans Spiro in New York

PROGNOSIS '95

SECURITIES INCLUDES CREDIT AGENCIES



POSITIVES

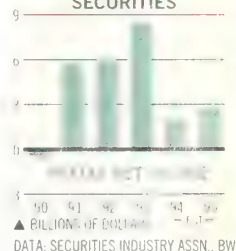
- Mergers and acquisitions remain strong.
- If enacted, a capital-gains tax cut and a tax deduction for IRAs would boost brokerage activity.

NEGATIVES

- Rising interest rates are driving investors to the bond market, dampening retail sales of stocks and stock mutual funds.
- A big stock market decline could send investors to the sidelines.

SPOTLIGHT

SECURITIES



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NEC

BACK FROM THE LAND OF THE LIVING DEAD

The tombstone over the commercial real estate market has started to move

PROGNOSIS '95

REAL ESTATE & CONSTRUCTION



POSITIVES

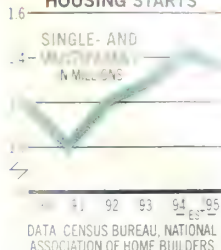
- Office properties will enjoy steady gains in occupancy.
- Commercial property values should improve as pension funds and others funnel more money into real estate.

NEGATIVES

- Higher interest rates will lead to a slowdown in the housing market.
- REITs will find competition for new properties tough and raising capital in the public markets even tougher.

SPOTLIGHT

HOUSING STARTS



It looks as though Samuel Zell was right. When the Chicago-based investor coined the phrase "Stay alive 'til '95" four years ago, the line became a mantra for the nation's beleaguered real estate executives. And sure enough, as 1995 approaches, commercial real estate is back. The new year should bring continued declines in vacancy rates and the first signs of rent hikes on some properties. And while higher interest rates will cause a slowdown in the housing market, new-home construction and sales activity should not fall off drastically—barring a huge jump in rates in 1995.

Last year, homebuilders racked up their best performance since 1986, despite an increase of almost two points in 30-year fixed-mortgage rates. Single-family housing starts hit 1.18 million. That's close to a 5% jump over 1993's showing, according to the National Association of Home Builders (NAHB). And the National Association of Realtors (NAR) puts 1994 sales of existing homes at around 3.98 million—also a jump of about 5%.

Sustained health in housing will hinge on how far interest rates rise. The NAHB expects the average fixed-rate mortgage to level off at about 9.5% in 1995, up from the current 9.15%. As a result, single-family housing starts should fall to 1.09 million, and sales of existing homes could drop to 3.73 million. The NAR predicts that housing prices will continue a modest climb, gaining about 4.5% nationwide, to a median price of \$115,400. Gains should be stronger in such fast-growing markets as Denver and Salt Lake City. But if mortgage rates top 10%, "we'd see a significantly weaker market," warns John A. Tuccillo, NAR's chief economist.

Construction of apartment buildings was also up in 1994 after years of decline. According to the NAHB, construction was begun on 247,000 apartment units, and an additional 275,000 should be started in 1995. A favorite among real estate investors, apartment properties have seen their prices climb steadily. The rich price tags on these properties are leading savvy investors to expect less impressive gains in 1995. Says Douglas A. Tibbetts, president of Equitable Real Estate Investment Management Inc.: "I'd issue an ex-

treme warning in certain markets," such as Denver, Las Vegas, Phoenix, and Tucson.

The battered office sector stands to make headway in '95. After two years of vacancy rates of close to 20%, the glut of office space built in the mid-1980s is finally being worked off. Downtown vacancy rates slipped to 17.7%, while suburban rates are 17.3%, according to Cushman Wakefield Inc.

With little new office construction, vacancy rates, particularly in the suburbs, will continue to fall. Cushman & Wakefield Chief Executive Arthur J. Mirante II says selected markets, such as Boston, Atlanta, and Portland, Ore., could actually see some rent increases. Industrial properties have also seen improved occupancy and rent hikes may follow in 1995 in such markets as Cincinnati and Charlotte, N.C. But the recovery will be gradual, and some urban office markets, such as Los Angeles, will continue to struggle as companies shun expensive new leases.

At the top of most lists for 1995's big winners are hotels. While there's still a room at the inn, occupancy levels are up for most market segments, and rates are climbing. "Hotels got slammed the hardest and are recovering the fastest," says Equitable's Tibbetts.

Much of this recovery is because of the return of capital to the real estate market. Banks are lending, pension funds are on the prowl, and investment banks are buying or making real estate loans to pool into securities for sale. And foreign investors from Europe, Hong Kong, and Latin America are expected to continue the fast investment pace.

All this may be bad news for the publicly traded companies known as real estate investment trusts. With better returns available through fixed-income investments, REIT shares, usually valued for their high yield, have tumbled.

For most players, though, the long-awaited recovery is here. "The industry is euphoric," says Lehman Brothers Inc. analyst S. Michael Giliberto. If the economy sidesteps a major slowdown, real estate execs will find even more to smile about in 1995.

By Amy Barrett in Washington

We don't condone a life of crime.



But we do think of Corsica
as somewhat of a steal.

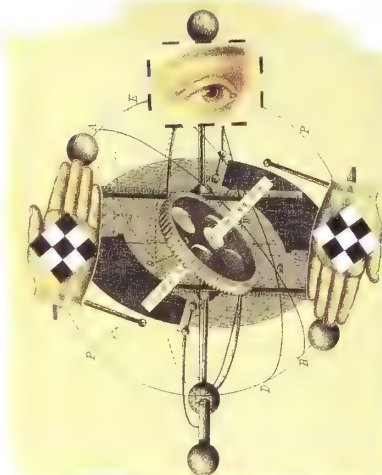
Imagine buying your new fleet vehicles from someone else and finding out that they can't compare to the value of the Chevy Corsica. You'd probably feel like you were fleeced. While others may charge more for the extras you want, Corsica costs less and comes with lots of important standard features, including anti-lock brakes, driver's-side air bag, automatic transmission, and even air conditioning. Corsica also has room for five passengers and 13.5 cubic feet of cargo space in the trunk. Choose Corsica for your fleet and get more for your money. You might call that pulling a fast one. We call it Genuine Chevrolet. To find out more, call us at 1-800-FLEET-OPS (353-3867).



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v jobs. Shifting

o 1995, the economy is healthy and buoy-
, even if Wall Street remains grumpy.
orporate America had one of its best years
r, and all the time and effort over the
t decade that went into getting lean and
an paid off big.

n the following pages, you'll see some
hlights from the past year. These are the
ults of a BUSINESS WEEK poll of its edi-
s around the world, who were asked to
ninate the year's most captivating man-
rs, entrepreneurs, and products. You'll

also read about
executives who
should be
watched for ma-
jor accomplish-
ments in 1995.

Inside, you'll
find a brilliant
CFO who is help-
ing to restruc-
ture the phar-
maceutical

industry. A canny Finn leading one of the
world's top cellular phone companies. A CEO
breathing new life into a former hot-prod-
ucts outfit that lost its way. A Japanese
entrepreneur angling for a piece of the
American action. And those fantastic prod-
ucts! Snazzy new cars and trucks. Powerful
multimedia computers. Engaging CD-ROMS
and great software for managers and kids.
Even a VCR that sets its own clock, at last.
Here are some of the outstanding achieve-
ments of 1994.

CALLING DR. LEWENT...

▼ Merck & Co.'s chief financial officer, Judy C. Lewent, made it painless. Swallowing drug distributor Medco Containment Services could have given Merck a huge case of financial indigestion in 1994. But by using \$4.2 billion in stock and just \$2.4 billion in cash—much of it borrowed—Lewent deftly spread out the financial impact. Merck's net income gains have hovered from 8% to 11% for the past six quarters, thanks in part to the 46-year-old, MIT-trained Lewent.



FAST MOVER FROM FINLAND

► Nokia Chief Executive Jorma Ollila is one of Europe's new breed of manager. In 1994, he led his \$4.6 billion Finnish mobile-communications maker to second place, right behind Motorola Inc., in world markets. The 44-year-old former Citibanker pushed Nokia to focus on customer service and technology. The result? Nokia stock soared 500%.



BURGER CRUSADER

► How do you say Big Mac in Arabic? Just ask 51-year-old James R. Cantalupo, president and CEO of McDonald's International. In the first three quarters of 1994, he opened 392 outlets overseas, compared with 280 launches in the U.S. Cantalupo helped boost profit margins to 21.6% in 1994 in company-owned stores, up from 20.8% five years ago. McDonald's has one restaurant per 29,000 consumers in the U.S. vs. one per 600,000 worldwide. Cantalupo has a lot of Golden Arches to build. Timbuktu, anyone?





BUT CAN HE MAKE PEACE?

▼ Talk about management challenges. In his first full year of power, Yoichi Morishita, the new CEO of the world's largest consumer-electronics company, Matsushita Electric Industrial Co., not only had to jumpstart domestic profits but also quell a rebellion in Hollywood. The first nonengineer to head Matsushita (he rose through sales), the 60-year-old Morishita boosted operating profits by 51%. Now he must make peace with MCA Inc., where the Americans want out.



OTHER STAR TIED DESI

brought back 3M's hit
e. The company that
s Post-its and floppy
stumbled in the '90s.
Executive L. D. DeSi-
streamlined the com-
development pro-
cutting in half the
takes to get prod-
market. It paid off
4.3M sales grew 7%,
9 billion, dwarfing
lled 2% average annu-
vth of previous years.
should hit \$1.3 bil-
5.5% increase. And
Desi, as he's affec-
ely known around the
aul (Minn.) headquar-
ers, believes profits
could be up 10%.





A BOOMING LATE BLOOM

Seventy-year-old trude Boyle not only chairs Columbia Sportswear, the world's largest maker of ski jackets, she also sets its image. gling with bikers at she appears in Columbia ad campaign as an off-bearing taskmaster working: In 1994, the Portland (Ore.) company's sales jumped 38%, to \$100 million, putting the 70-year-old Boyle ahead of Patagonia.

PLOWING IN PLOWSHARE

Donald R. Beall Jr. finally weaned Rockwell International Corp. from the government. His \$1.1-billion acquisition of Cleveland's Reliance Electric Co. means Rockwell now derives only 18% of its revenues from military contracts. For 1994, the company well earned \$634 million, a 13% jump over 1993. 56-year-old Beall posted a 20% return on shareholder equity for 1994.

MANAGERS TO WATCH IN 1995



GROVE

Andrew S. Grove is on the hot spot. The 58-year-old chairman of Intel is facing the biggest challenge of his career as a glitch in the new Pentium chip causes major customer concerns. Intel agreed to replace all chips only after weeks of mounting customer criticism—and a hammer blow from IBM. Grove must transform Intel's technically oriented culture into a customer-focused service culture. And can ex-Disney exec Jeffrey Katzenberg create a real company of his own? As the

prime mover in a newly created production company with superstar director Steven Spielberg and record mogul David Geffen, Katzenberg will spend most of early '95 building alliances to raise the nearly \$2 billion he'll need for a Hollywood studio. After stints throughout the Coke empire, M. Douglas Ivester, chief financial officer of Coca-Cola Co., was elevated to president/coo status in July. That makes Ivester as heir apparent to CEO Roberto Goizueta. But can down-home Doug, shy numbers maven, fill the shoes of the sophisticated Cuban-born aristocrat?



KATZENBERG



IVESTER



MUSTANG ALEX

▼ He has been at the helm of Ford Motor Co. for only a year, but Alexander J. Trotman has the carmaker humming. With plants running at the highest rate of any of the Big Three, he's adding output of Explorers and cranking out a new line of minivans, without the strikes that have hindered rival General Motors Corp. Trotman, 61 years old, saved the classic muscle-car Mustang from the junkyard and used it to help boost Ford's profits to \$3.7 billion in the first nine months of 1994 on sales of \$95 billion. Trotman launched "Ford 2000" in 1994 to reengineer the long-time multinational along global lines. Europe gets to develop small cars, Detroit the rest.



a year at the helm of Kodak, George s already made a difference. Selling the health operations refocused Kodak on its usiness and brought in more than \$8 bil- 95, Kodak will introduce new digital-imag- cts such as thermal printers, and prepare a 1996 launch of a new 35mm camera standard that could spark big sales. The magic hasn't worked at Kodak for many years. Can Fisher now become the magi- cian that he was at Motorola? Loida Nico- las Lewis, the widow of Reginald Lewis and current chairman and CEO of TLC Beatrice, is eyeing 1995 as a possible time



LEWIS

to take her company public. But first she must generate some profitable quarters. 52-year-old Lewis' strategy is to pare costs low enough and ride the European recovery. Richard Parsons knows all about pressure. As chairman of Dime Savings Bank of New York, the 46-year-old lawyer helped rescue the thrift from insolvency. Now, Parsons is parachuting into the presidency of Time Warner.

Chairman Gerald Levin has placed an enormous bet on cable TV's abil- ity to deliver interactive and phone ser- vices. Levin wants Parsons to be an ad- vocate of Time Warner's strategy on Wall Street. Can he do it?



PARSONS



MUSIC-BIZ MILESTONE

▲ Time Warner Inc.'s music group generated plenty of bad vibes in 1994, as Chairman Robert J. Morgado feuded with his record-label executives. But Sylvia M. Rhone continued making sweet music. In taking over Warner's Elektra Entertainment, Rhone becomes the music industry's highest-ranking woman and African American. The 40-year-old graduate of the Wharton School began as a Wall Street investment banker.

MANAGERS TO WATCH IN 1995



EATON

Robert Eaton's first big challenge as Chrysler's chairman is simple: clean up his company's uneven quality. Eaton has tried, but the company still lags. J. D. Power & Associates pegged all Chrysler brands below average in 1994's defect ranking. Then the January, 1995, *Consumer Reports* yanked an earlier endorsement of the Dodge Intrepid sedan.

Eaton must act fast. So must Goldman Sachs's Senior Partner Jon Corzine. Profits are down,



CORZINE

senior partners are leaving, and the once conservative firm's jump into aggressive proprietary trading is backfiring. Corzine must cut costs and restore the luster to what once was Wall Street's most profitable house.

Andrew Grove's Pentium problems may be Jerry Sanders' opportunities in 1995. By midyear, the CEO of Advanced Micro Devices expects to ship the K6 microprocessor—AMD's rival to the Pentium. Sanders is making the biggest gamble of his career: With no backup based on Intel's designs, he's betting the company on the new chip.



SANDERS

THE GATES JUGGERNAUT

▼ What a year for Bill Gates! The Microsoft Corp. CEO beat the Justice Dept. on a monopolistic-pricing rap, then announced plans to buy rival software maker Intuit Inc. for \$1.5 billion. He also spent \$30 million for a Leonardo da Vinci manuscript and found time to get married. Gates marked 1994 by shifting Microsoft into consumer markets such as home-finance management and multimedia. Oh, yes, sales and profits are way up.





Caravaggio - *Il Ragazzo con la Lute*

COMMUNICATING IS AN *A*RT

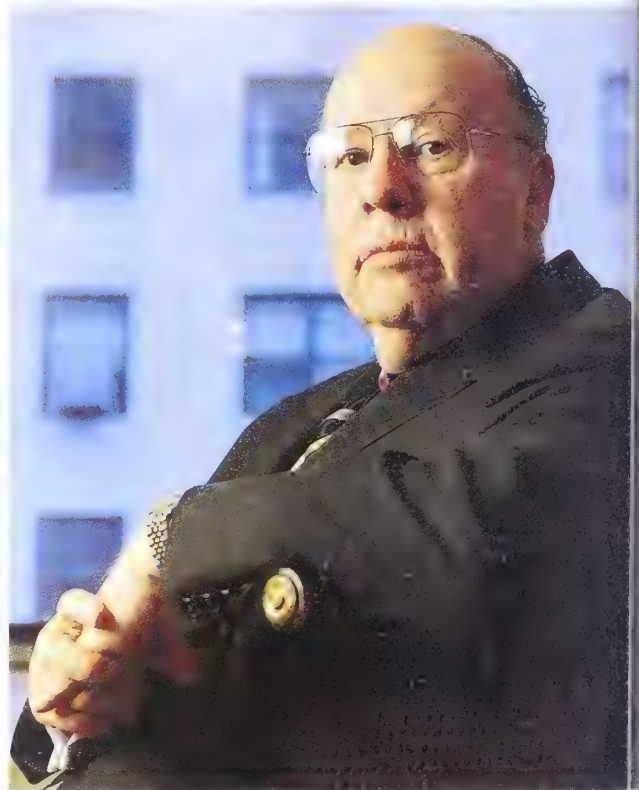


TELECOMMUNICATIONS
IN ITALY AND THE WORLD



STAINLESS RESULTS

▼ Big Steel did great in 1994, but Thomas Graham, CEO of AK Steel Holding Corp., did the best. Graham took his company to the head of the industry, earning more per ton than anyone else. Taking over in 1992 after being passed over for the top job at U.S. Steel—Graham cut costs and pushed more steel through the remaining lines. Output per worker rose a staggering 58% in two years. The payoff came in 1994, when profits are estimated to hit \$100 million on sales of \$1.9 billion. That allowed Graham, 67, to take AK Steel public: As most steel stocks languished, AK became the darling of Wall Street.



WOWING 'EM ON THE STREET

▲ While the billionaire chairman of Viacom Inc., Sumner M. Redstone, grabbed the spotlight during his epic takeover battle for Paramount Communications Inc., his president and CEO, Frank J. Biondi Jr., worked to ensure the consolidation of the Viacom empire, which included Blockbuster Entertainment Corp. Biondi tackled the \$10 billion debt by signing a deal to sell Madison Square Garden Corp. for a cool \$1 billion and entering negotiations to sell Viacom's cable systems for an additional \$2.4 billion. Wall Street was impressed. Now it's waiting for Viacom to make another move—perhaps taking over one of the nets.

MANAGERS TO WATCH IN 1995



FORD

Would you rather be chairman or CEO of Ford Motor Co.? By becoming head of the board's finance committee on Jan. 1, William Clay Ford Jr., 37, opted for the first. The man once referred to as "Billy" will now oversee all major financial decisions. Watch him. And while you're at it, keep an eye on Edward R.

McCracken, CEO of Silicon Graphics Inc. SGI made its fortune building 3-D graphics computers that created the dinosaurs in *Jurassic Park*.



MCCRACKEN

Now, McCracken wants to make SGI a household acronym. Time Warner Cable's interactive-TV trial in Orlando—for which SGI designed the set-top boxes and servers—is under way.

Nintendo also will unveil its next-generation SGI-designed video game. Can McCracken's strategy work? Daniel P. Tully, chairman of Merrill Lynch & Co., thought his had. Merrill had a boffo year in 1994 while other Wall Street houses were getting whacked. Then came the shocker: Merrill sold those derivatives to Orange County, Calif. Can Tully protect Merrill and keep the gains?



TULLY

COMMUNICATION. THE ART OF BRINGING TOGETHER PEOPLE, NATIONS AND CONTINENTS.

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always been a nation of the arts -everyone knows it- but
today, there's another art in which Italy is an acknow-

ledged world leader - the art of communication. The Italian Telecommunications System is a world-wide network of vital importance.

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The STET Group operates in all sectors of telecommunications: from services to manufacturing, from information facilities to multimedia

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people to exchange and collaborate ever more efficiently. The STET Group is a market orientated company quoted on the stock exchange

and whose stock is owned by thousands of shareholders. It is one of the largest companies in the world with 140,000 employees, a

revenue of \$20 billion and \$5 billion in investments. The STET Group activities reach out beyond its national boundaries, spreading

Italian technology and know-how throughout the world. Like the arts, telecommunications bring together people, nations and continents.



TELECOMMUNICATIONS
IN ITALY AND THE WORLD

BIG BLUE'S FINANCE CZAR

▼ Louis V. Gerstner Jr. gets credit for IBM's return, but Jerome B. York, the new, blunt-talking finance chief, engineered a balance-sheet turnaround. By cutting costs ruthlessly, the 56-year-old pushed Big Blue into the black for four quarters and piled up \$11 billion in cash. No wonder IBM's stock is in the 70s—20 points higher than when he and Gerstner took over.



HARD-EARNED COMEBACK

► It took four painful years, but in 1994 Jerome J. Meyer finally turned around venerable Tektronix Inc. in Wilsonville, Ore. Earnings are up 60%, and the stock recently hit 40, nearly doubling in a year. Meyer's strategy has been to pare Tek from 23 divisions to just 4, cut employment by half, and focus on new products: The hottest is color printers, where Tek dominates the high end. Tek also has strong new offerings in video-display terminals and equipment for TV production and testing. Even its old mainstay, test and measurement gear, is growing again, as the 56-year-old focuses on the fast-growing telecom market.



FOR HIS NEXT MIRACLE...

▼ He did it once and then again. Allen I. Questrom confounded skeptics when he took over Federated Department Stores Inc. and successfully led it out of bankruptcy. Then, in 1994, he merged Federated and bankrupt R. H. Macy & Co. into the largest department-store chain in the U.S.—a \$14.5 billion titan.



APPLE POLISHER

▲ For Michael H. Spindler, it was the year of living pragmatically. In 1994, Apple Computer Inc.'s new, no-nonsense CEO proved that his no-frills style was just what the freewheeling but ailing computer maker needed. The 52-year-old Spindler, nicknamed "the diesel" for his hard-charging ways, pared cost and made Apple efficient enough to go keyboard-to-keyboard with Compaq Computer Corp. Then he launched the first all-new Macs in more than a decade: the Power Macintoshes, whose sales are ho

capability: executive programs

DRIVING CAPITALISM



Illustration by John Labbé. As seen in Business Week, April 19, 1993 issue.

Note Speakers:

GEORGE BUSH
Former President of the
United States of America

BOB BARNEVICK
Chairman and CEO,
a Brown Boveri

THE HONORABLE RONALD BROWN
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The 1995 Business Week Presidents Forum

21st Century Capitalism: New Rules for the Global Economy

At the Bob Hope Chrysler Classic

Date: February 15-18, 1995

Place: Hyatt Grand Champions, Indian Wells, California

SIGNIFICANT ECONOMIC AND POLITICAL CHANGES around the world have opened doors to new global markets. Today's corporate leaders must tread quickly and with confidence to achieve success in these uncharted waters.

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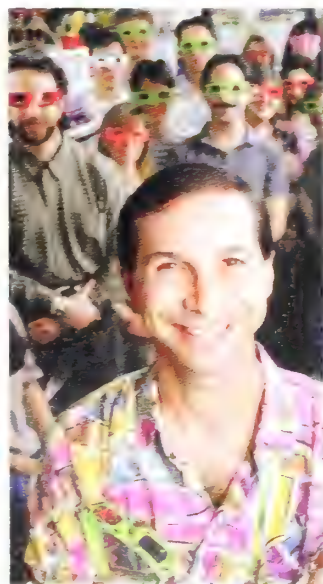
BusinessWeek

Beyond news. Intelligence.



OPERATION BOOTSTRAPS

▲ In the wake of the Los Angeles riots, Crenshaw High School students found a way out of the streets. They came up with Straight Out 'the Garden All Natural Creamy Italian, a bottled salad dressing that is now in 2,000 California groceries. Nearly \$35,000 has been set aside for college scholarships.



PEANUTS. NOT!

▼ Scott D. Cook's share of the \$1.5 billion buyout by Microsoft Corp. of his Intuit Inc., the home-finance software company he founded, should come to a cool \$300 million.



PLUG AND PLAYROOM

▲ Bill Gross, founder and chairman of Knowledge Adventure Inc., knows that parents want software to help their kids explore. Sales of his La Crescenta (Calif.) company tripled in '94, to \$35 million. Steven Spielberg loved it. He bought in.

IN THE RUST BELT, LIFE'S A NICHE



RUSHING THE NET

► James H. Clark, co-founder of Silicon Graphics Inc., is going for an encore: paving the way into the Internet. His Netscape Communications Corp. software is 10 times faster than Mosaic. Clark, who is 50, may luck out. William H. Gates III's Windows 95 software, which will give instantaneous access to the Net to millions of PC users, is delayed until August. Netscape shipped Dec. 15.



HARDBALL IN SOFTWARE

▲ Japanese software mogul Masayoshi Son did not win the prize in 1994, the computer magazines sold by Ziff-Davis Publishing Co., but the 37-year-old Korean immigrant did put himself on the map. He built his \$2 billion company, Softbank Corp., into Japan's biggest software wholesaler, linking up with both Microsoft and Novell. Son went to the University of California at Berkeley.

◄ Matthew W. Botsford is building the first new steel mill in Pittsburgh since World War II. It's a \$400 million project. Botsford's WorldClass Process makes niche products that even Steel won't touch. He just make more of them.

THEME.



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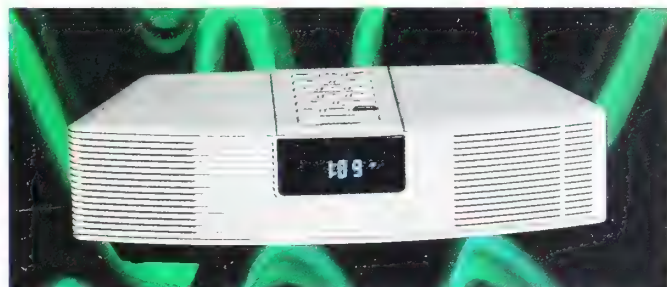
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MAXIMEDIA

► There is nothing cooler than Packard Bell Electronics Inc.'s multimedia computers. The new PCs come packed with cable-ready TV, an answering machine, fax, stereo radio, and a CD-ROM drive that can play either audio CDs or the gobs of software that are included in many models. Price: about \$2,000. After years of hype about Information Appliances, they're here.



SONIC BOOM

◀ A clock radio for \$349? Yup, and Bose Corp.'s WAVE radio sounds every bit as good as you'd expect, given the price. Using Bose's advanced wave technology instead of conventional speakers, it produces impressive fidelity in a surprisingly tiny box. A pleasant design and a nifty remote-control add to the fun.

A WHOLE NEW OLDS

▼ A stylish, hot-selling Oldsmobile used to be an oxymoron. No more. Its new Aurora is selling like crazy. Buyers love the luxury sedan's knockout styling, comfy ride, abundant standard features, nimble handling, and powerful V-8 (son of Northstar). It starts at \$33,700, vs. \$51,000-plus for Toyota's Lexus LS 400.

THE FANS ARE PAGING WILL

▼ When (and if) the baseball season starts, check out Motorola Inc.'s SportsTrax, a pager that allows aficionados to follow the home team. SportsTrax shows the score, base runners, and the number of outs. For \$200, fans buy the pager and three months of service. Motorola rolled out the first set for Toronto Blue Jays fans, who had about those Jays,





SMALL STEP FOR A ROBOT

700-lb. Dante II robot hefted itself up on its side in August and walked straight down into a hell—the Spurr volcano in Alaska. In an experiment aimed at proving the usefulness of small, cheap robots in dangerous missions from earth to Mars,

Dante took gas samples and video pictures of the entire crater area. The \$1.7 million robot was built by Carnegie Mellon University scientists. In the end, however, the robot needed a helicopter rescue—after tipping over on its side.

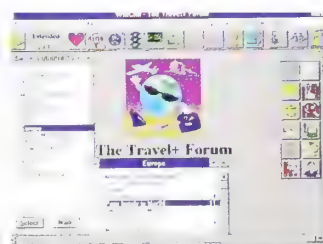
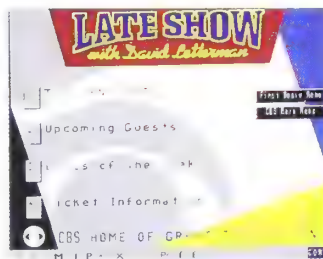


WRIST SMARTS

▲ Calling Dick Tracy. The Seiko MessageWatch is an \$80 watch-beeper. You can get the S&P index and the Dow Jones industrial average transmitted at the market close, local sports scores, and weather. Soon it will keep you when your stocks go beyond preset minimum and maximum prices. Wow!

A MIGHTY SWEET SPOT

▼ Are those oversize fat woods sending you into the sand instead of onto the green? Taylor Made Golf Co.'s midsize woods are only 18% larger than a standard club but offer a much bigger sweet spot. Midsize clubs are selling and so is Taylor Made's fairway driver and 7-wood (\$180 for graphite).

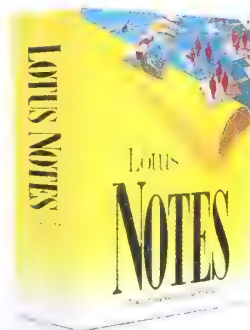


ONLINE GOES MAINLINE

◀ When Jerry Seinfeld goes online to meet fans via E-mail, you know the Info Highway has arrived. Cyberspace isn't just for pencil-packing geeks anymore. It's the hottest way to communicate, especially with customers. Companies stormed the digital kingdom in 1994. Catch *Time*, *Newsweek*, and *BUSINESS WEEK* online. Shop for L. L. Bean outdoorsware. Even the White House is pitching over the wire. The big winners from top down: Prodigy, America Online, and CompuServe. Membership is soaring, and companies are piling on.

NET WORKER

▼ Mosaic turns the arcane Internet into a medium for the masses. It lets you zip from colorful weather maps to the Rolling Stones and then order roses—without typing a single command. Price: free off the Net.



HARMONIOUS

▲ It's hot and keeps getting hotter. It's Notes, Lotus Development Corp.'s "groupware" program that helps teams collaborate and share data. Nobody does it better. Price: \$300 per copy.



FINN PHONE

▼ Road warriors love Nokia's 2100 series digital mobile phones. Their PC Card accessories can send and receive data, fax, and E-mail. The Finnish phone has a 3-ounce fast charger and costs about \$400 with monthly service.



DOUBLE EXPOSURE

▲ Nikon Corp.'s \$425 N-50 35mm SLR has two exposure modes. Simple mode turns the N-50 into a point-and-shoot camera. Advanced has settings for night-time, sports, and other situations.

MYSTICAL QUEST

▼ This CD-ROM has a cult. Beautiful, puzzling, and mysterious, *Myst* (\$55) avoids the usual CD scene of sex and violence to offer a surreal world of shipwrecks and symbols.



VCRs: NO MORE FLASHING 12:00

▲ At last! A VCR clock works. Sony's new SLV-770HF (\$599) and its SLV-920HF (\$649) models contain a chip that reads time code broadcast by stations over a part of the television signal that is





ved for data services. permits the VCRs to automatically set their own clocks. So you don't need a teenager to get the VCR clock to stop running anymore. It's a new way to impress your friends and neighbors. For all these years, no more clock!

DONKEY KONG CHRISTMAS

▼ In its first week in the U.S., Donkey Kong Country sold 500,000 copies. British brothers Christopher, Stephen, and Timothy Stamper created this Christmas best-seller for Nintendo Co. They used Silicon Graphics Inc. computers to develop a 16-bit game that has mesmerizing animation and a wonderful feel to it. Price: \$49.95.



CALLING-CARD CRAZE

▲ They're becoming collectors' items. Prepaid phone cards, initiated in Europe, are gaining in the U.S. Cards come in any denomination, are easy to use, and allow young adults to gain a handle on their own talk time.

SUMPTUOUS SCUBA

◀ Nekton Pilot boasts a seasick-resistant ride, an adjustable diving platform, cabins with picture windows, plus private showers. Cost? \$1,350 for a week-long scuba trip.



POWERPC TRIP

▲ Look out Pentium, the PowerPC chip is going gangbusters, driving the Power Macintosh into the sales stratosphere. The blazingly fast PowerPC—a product of an Apple-IBM-Motorola partnership, makes the new Macs eight times faster than their predecessors when using new software. Price: \$1,819 and up.

PORTA-BIKE

► Don't let the small wheels fool you. Bike Friday's Pocket Rocket is a lightweight, American-made high-tech racer that folds to fit in a suitcase for traveling. Green Gear Cycling in Eugene, Ore., builds them for the road or trail—even a tandem. Price: \$1,250.



FAX PLUS

▼ It won't take dictation, but it does everything else. Hewlett-Packard Co.'s new Office-Jet combines a plain-paper fax, a copier, and a computer printer into one machine (\$750 at discount). It's a great space-saver for the home office.



BEAUTIFUL BUT SHALLOW

▼ Home theater keeps getting better. The new Slim Design Projection TV from Thomson Consumer Electronics has a 52-in. screen without the bulk: It's only 21½ in. deep. Price: \$2,899.



TEMPTING DISH

▲ Want movies, sports, and great picture quality? Try the RCA Digital Satellite System. At \$900, it's a hit—nearly 500,000 already sold by Thomson Consumer Electronics. DSS has a large-pizza-size satellite dish plus decoder box. Downside? No local channels.

EURO RIDE, AMERICAN SPACE

▼ The Cirrus takes Chrysler Corp.'s groundbreaking "cab-forward" design to new frontiers. This compact has the nimble handling of a European sport sedan and the interior space of a much larger car. The LX starts at \$17,970, comes standard with a 2.5-liter V-6, automatic transmission, and antilock brakes. The top-end LXi stickers at \$19,900, with many goodies standard. But can it beat the new Ford Contour?





THEY BRAKE FOR SKATERS

▲ Move over ABS, here come ABT brakes—on Rollerblades! Automatic Braking Technology on the \$400 Bravoblades makes stopping easy. The wheels don't have to leave the ground to brake.

BLAZER ON A BURN

▼ Chevy's new Blazer (and its sister the GMC Jimmy) are General Motors Corp.'s first serious contenders in the red-hot compact-sport-utility market. Its sleekly rounded styling, quiet ride, and sophisticated manners are winning over urban and suburban cowboys. But Blazer is no sissy: Its V-6 engine is brawny. At \$18,955, Blazer is cheaper than most others in its class.



PRODUCTS TO WATCH IN 1995

■ The Ford Taurus and Mercury Sable, which launched Ford Motor Co.'s mid-'80s renaissance, get their first major restyling in 1995. Out goes the aerodynamic look, which let the cars slice easily through the air. In comes a more muscular "bio-kinetic" look. Speaking of "looks," Microsoft

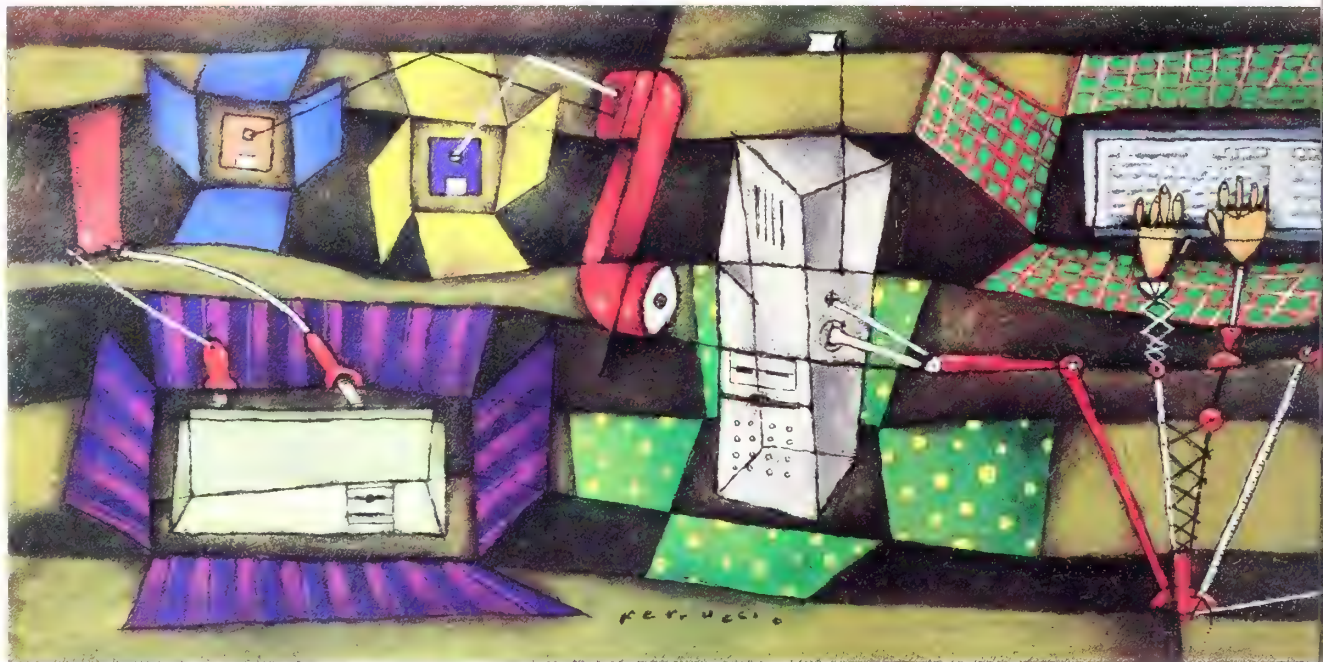


Corp.'s Windows 95 is supposed to make IBM-compatible PCs look better than the Macintosh. It will make computers easier to use and include its own online service, Microsoft Network, which will plug consumers into games, news, and E-mail for a monthly fee. Price: \$100 retail. Too bad it won't be out until



August. Wouldn't it be cool if we could connect to the Net on the go? Magic Cap, software by Silicon Valley startup General Magic Inc., allows you to send and receive E-mail, faxes, and phone pages by tapping on the screen of a handheld device. So far, only Sony Corp. has one, the \$995 Magic Link.





EDITED BY AMY DUNKIN

WHEN YOUR PC CRIES OUT FOR THE EMERGENCY SQUAD

This is the "slowest computer I've ever seen in my life." The caller, named George, was flummoxed. His week-old Packard Bell 486 was hobbling along at such a lethargic pace that even his old 286 PC ran faster. George's cry for help was made to Packard Bell's support center in Magna, Utah. Phil Seifert, the rep who answered the call, asked George to identify the color of a light in the front of his machine. Told amber, Seifert instructed George to push a button that changed the light to green and transformed the machine into "turbo mode." George was then asked to reboot. Voilà—case solved. The call took less than eight minutes.

Unfortunately, not all tech support calls are handled with such dispatch. PC owners are quick to pass along war stories of constant busy signals or endless "please be patient"

messages as they languish on hold. The sad truth for those who have recently unwrapped new PC gear: You need not be a Pentium owner with a long-division problem to face such a predicament.

Those seeking proof that Murphy helped Santa pick out their computers this Christmas should consider the dilemmas consumers face. Maybe the sound doesn't work. Perhaps you

aren't able to get a new flight simulator off the ground because you can't free up enough memory. You might have a fax modem that gives but does not receive. Or maybe your system has crashed and you can't get anything running at all.

Although most computer companies promise to back up their wares with some degree of technical competence, the types of service and reliability

vary widely. Some support people sound like politicians—quick to place blame elsewhere. Hardware reps might claim the fault lies in a piece of software; the software company blames the computer manufacturer. Both may throw darts at Microsoft Windows. Companies are starting to admit that all the customer wants is a solution. "We'll take

ownership for the problem," insists Brent

Cohen, chief operating officer of Packard Bell.

Many hardware companies offer toll-free technical support, and some such as Apple, Compaq, Dell, and IBM are open 24 hours. Still, you may have a lengthy wait before you get through to a human being. Before buying any PC, consumers should check out tech support lines. Even outfits that are quicker to put you in touch with a live voice

may make you pay for a privilege, either by running up long-distance charges, using a credit card, or dialing a 900 line.

PLEASE HOLD. Gateway 2000, a major mail-order computer dealer, has always boasted competitive prices, though some customers may become frustrated by the company's service. Gateway has set up a dedicated service number for its major accounts. "Our goal is to answer the call after a few rings. On the consumer side, however, the chances of getting through rapidly are iffy. Gateway claims the average wait time is about 10 minutes, though it can be much worse. Robert S. Keefe, a New York communications consultant, says he recently tried Gateway's tech support number 120 times and got an answering machine without an outgoing message only, adding that "unfortunately" he

COMPUTERS



Computer companies promise to back up their wares—but service and reliability vary widely

staff was too busy to accept calls. Keefe finally called the sales department and reached a supervisor after threatening to return the machine. Despite such incidents, Gateway, along with Compaq, Dell, Digital, Hewlett-Packard, BM, Micron, Northgate, and EOS, got top grades of A in

PC Magazine's latest service and reliability reader survey.

Packard Bell, on the other hand, received an E, the lowest in the survey. But the company, which sells machines through mass-merchant retailers, is trying to bolster its reputation. At present, some 900 technicians

handle 14,000 calls a day. The company takes hardware-related calls on a toll-free, 24-hour line; those with software problems must call Utah on their own nickel, at reduced hours. Packard Bell is aiming to reduce the average time it takes to answer calls from nine minutes to two.

For many customers, the most infuriating thing is that some companies provide telephone service only during business hours, when most people are away from their home computers. Mark Skapinker couldn't get Disney's *The Lion King* software he brought home for his 6-year-old son to work one Saturday. The program failed to detect the sound card inside his machine. But Disney's support line was closed until Monday. "My kid is yelling at me because, of course, he thinks it's my fault," says Skapinker, president of Delrina, a Toronto software company. Delrina's own tech support line is not open on weekends either.

As an alternative during off-hours, most companies have a strong tech support

presence in cyberspace. You can usually find company reps in forums on CompuServe, the Internet, or a company's own bulletin boards. People can also send and receive technical queries at many companies, including Dell and Gateway, by fax.

Luckily, tech support is getting more sophisticated. IBM and Compaq can tap into your PC by modem and download software fixes or alter your "autoexec.bat" and "config.sys" files. A "queue jockey" at Microsoft can tell you how long your wait will be.

Long gone,

however, are the days when computer makers could be counted on to provide such help gratis. Increasingly, software companies grant customers only 30 to 90 days of free help, asking them to pay later. In general, during the free period companies will provide advice on setting up and using the software, as well as fixing things that go haywire. But there's a fine line between a legitimate call for help (i.e. something is broken) vs. getting a lengthy tutorial on how to set up business on a spreadsheet, say. "If somebody called us time and again for games counseling, that's where we would draw the line," says Deborah Willingham, vice-president for support at Microsoft.

CLUELESS. Some third-party companies sell service plans to individuals. Digital Equipment (800 722-9332) offers *Service-in-a-Box*, providing unlimited, toll-free support for business software from publishers such as Adobe, Lotus, and Symantec. The price is \$144 a year. For \$50, Corporate Software (800 477-7450) allows calls on five problems concerning any of 50 top-selling business programs.

But these services may not be the best choice for most home users—they don't cover multimedia games, for one thing. The packages make sense only for those who run a lot of business programs at home and are often under a time crunch. In fact, if people took the time, many could find answers to most questions by consulting onscreen "help" files or the manual.

With the influx of PCs into homes, more novices are flooding support lines. Lest you think you are the only one who is clueless, some people confuse a mouse with a foot pedal. Others, when reading onscreen instructions that say "press any key," ask where they can find the "any" key. And according to techie lore, some take the command "close the window" literally: They shut the window in the room. *Edward Baig*

How Tech Companies Handle Service

APPLE 24-hour, toll-free support. Fax-back service.

COMPAQ 24-hour, toll-free support. Fax-back service. Can diagnose and fix problems by modem.

CREATIVE LABS Customer pays long-distance toll, 7 a.m. to midnight Central Time, including weekends. Fax-back service.

DELL 24-hour, toll-free support. Automated phone line for common questions, and fax service.

IBM 24-hour, toll-free support line. Dispatches replacement parts within 48 hours. Fax-back service. Company can fix software on your PC by modem.

GATEWAY 2000 Toll-free support, Mon. to Fri., 6 a.m. to midnight; Saturday 9 a.m. to 2 p.m. Central Time. Fax service.

MICROSOFT Free support for most software, though customers pay long-distance charges. 6 a.m. to 6 p.m., weekdays, Pacific Time. Free support on Windows lasts 90 days, then charges are \$2 per minute, \$25 per incident, or \$195 a year.

NOVELL Six months of toll-free support on weekdays, 7 a.m. to 6 p.m. Mountain Time, on business software such as *WordPerfect*. Costs after are \$25 per incident or \$2 per minute, or up to \$425 for service package. Customer pays toll for support on consumer titles, 8 a.m. to 5 p.m. Mountain Time, weekdays. Fax-back service.

DATA: BUSINESS WEEK

CONSTRUCTION STOCKS: HIGH-RISE IN THE MAKING?

This past year, with developing nations in the midst of a building binge, you'd think investors would have raised the roof on construction stocks. Not so. Orders and earnings have been disappointing, sending shares down an average of 12.3% in 1994. But some stock watchers believe the sell-off has created bargains in infrastructure shares that could pay off in 1995. "This is the time that you buy these very-late-cycle stocks," says Tobias Levkovich, an analyst at Smith Barney. "These guys have built backlog to sustain earnings, even through an economic downturn."

The \$1 trillion construction boom unfolding in Asia (BW—Nov. 28) has set the stage for a resurgence in profit. Rising oil, chemical, and paper prices also portend good things, says Carey Callaghan, an analyst with Lehman Brothers. The producers of these industrial commodities will have to add to capacity at a faster pace if they want to grab market share. In addition, plant utilization is creeping closer to capacity, and machinery prices are rising, two more signs of construction work to come. Even Union Carbide, which has pledged to hold down construction spending, is building a \$1 billion petrochemical plant in Kuwait.

SUNNY PROSPECTS. The long view of global power markets is equally pleasing. General Electric forecasts that total new demand for electric power could reach 1,089 giga-

watts during the next nine years. At \$1 billion to produce each new gigawatt, a vast market may materialize. The U.S. power market, however, remains slowed by energy conservation, restrictions on capital spending, and industry restructuring.

A handful of contractors should be able to build profitable backlogs and improve margins in 1995. Fluor, the largest construction company in the U.S., also operates a moneymaking subsidiary that sells low-sulfur coal. Fluor has had five years of steady earnings growth and finished fiscal 1994, which ended Oct. 31, with net earn-

Foster Wheeler may be in an even better position to benefit from the world building boom. It earns 58% of its revenue outside North America through services that include building oil refineries and fabricating boilers used in power plants. While China no longer is the potential gold mine it once promised to be, Foster Wheeler is cultivating clients in India and Latin America. Soft orders in

the latter part of 1994 scared off some investors and sent the share price below \$30. But 1995 earnings should move up at least 15%, says Smith Barney's Levkovich.

Likewise, evaporating defense con-

much higher p-e multiple than the current conservative 11, which is average for a defense contractor.

Not every infrastructure company needs a boost from the global recovery, however. Some of them will prosper based primarily on domestic contracts. Jacobs Engineering Group, which works mostly in the U.S., upped its 1994 earnings per share 10%, to \$1.26, and should see them grow an additional 25% in 1995. And Jacobs booked several one-time charges in 1994 that are likely to pay off over the next several years. The biggest was for restructuring related to the acquisition of engineering and construction businesses of CRSS. The acquired company specializes in the design of microchip manufacturing plants and paper mills, two sectors where expansion is likely.

Increased activity among Jacobs' chemical clients should also help push earnings to \$1.57 per share during 1995.

The most intriguing prospect in the world's hard hats are hammers could be steel fabricator/erector Pitt Des Moines. Earnings per share

will hit at least \$3 again after an off year in 1993, but its stock price hasn't yet moved. The major drawback here is poor stock liquidity—the founding Jackson family owns 43%, and there are only 260 or so owners of record. But if you don't mind taking a small, potentially illiquid stake, the price, now around \$34, could hit \$50, says a Denburg Thalmann analyst Frank Prezelski.

That could nail down a nice profit for your stock portfolio. *Richard Korman*

SMART MONEY

SOME INFRASTRUCTURE INVESTMENT PLAYS

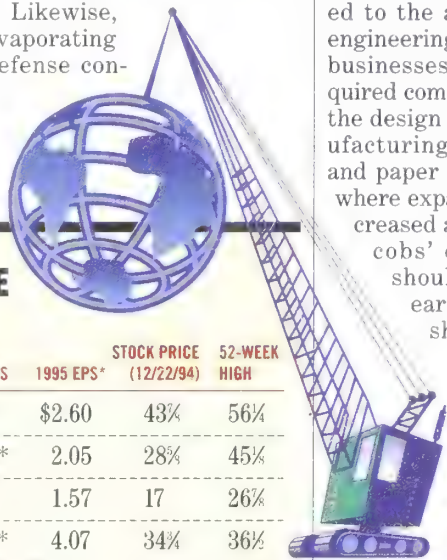
	1994 EPS	1995 EPS*	STOCK PRICE (12/22/94)	52-WEEK HIGH
FLUOR (FLR)	\$2.32	\$2.60	43%	56%
FOSTER WHEELER (FWC)	1.85*	2.05	28%	45%
JACOBS ENGINEERING (JEC)	1.26	1.57	17	26%
PITT-DES MOINES (PDM)	3.00*	4.07	34%	36%
RAYTHEON (RTN)	5.73*	6.34	63%	68%

*Estimated

DATA: LEHMAN BROTHERS INC., BLOOMBERG FINANCIAL MARKETS

ings per share of \$2.32. Earnings of \$2.60 a share are possible for 1995. Yet its estimated 1995 price-to-earnings multiple of 16.5 is well below its historic average. Fluor's biggest prize in 1994 was the prime contract on Union Carbide's Kuwait plant. But near-term prospects are particularly sunny in Asia, the Pacific Rim, and Latin America, says Chief Executive Les McCraw.

tracts have produced a more bullish outlook for Raytheon, which over the past few years has added several well-managed construction companies to its peace portfolio. In 1994, Raytheon purchased the construction arm of Ebasco from Enserch, making Raytheon one of the world's biggest builders. So CS First Boston analyst Peter Aseritis expects Raytheon's stock to trade in the future at a



Global recovery and a \$1 trillion Asian building boom have set the stage for a resurgence in construction profits

A positive a+++itude

It does seem as if India, the nation, has caught up with Essar, the corporation. Our belief in a positive attitude is today the preserve of an entire country. With good reason, too.

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ESSAR
INDIA

MAYBE JUST DEATH IS INEVITABLE

Death duties are the heaviest taxes the government imposes on individuals, intentionally designed to turn heirs of haves into those who have less. Many among the new GOP majority in Congress want to ease the burden slightly by raising to \$750,000 for individuals (or \$1.5 million for married couples), from \$600,000 (or \$1.2 million), the amount that can be excluded from estate taxes. But even if the rules aren't changed, loopholes in the existing laws are big enough to drive a Mercedes through. They are called trusts, and they can shelter some wealth even into the third generation.

There are trusts whose main goal is not tax avoidance but exercising control from beyond the grave—to prevent a ne'er-do-well child from squandering the funds, for example. But mostly, trusts are designed to elude estate taxes by enveloping assets in a kind of legal shrink-wrap. They don't have to be impermeable—many trusts can provide current income for you or your surviving spouse while shielding principal from the Internal Revenue Service. And the wrap can be highly elastic: Some \$100,000 worth of growth stocks in a trust for your 10-year-old child could, 40 years later when you die, be worth a tax-free \$2.2 million, assuming an 8% annual return.

The rules are complex.

Some trusts are revocable, becoming part of your estate at death. But only the irrevocable type are useful for tax avoidance. Probably the most common irrevocable setup is the life-insurance trust, which removes death benefits from a taxable estate. This trust has other advantages: It avoids probate, meaning the proceeds are immediately available to heirs. And it allows you considerable control over

insurance trust before buying the policy. Otherwise, if you die within three years of transferring an existing policy, the proceeds revert to your estate. Once you establish the trust, you can't borrow against the policy or change beneficiaries. And you must designate a trustee to manage the assets. To avoid having to pay gift taxes on the annual premiums, many people make the

children would not benefit from his \$600,000 estate-tax exemption after his wife died. The solution: Set up what are called A and B trusts, which would preserve the combined \$1.2 million exclusion for both parents.

HOME SECURITY. The way works is that the husband creates an "A," or marital trust for his wife and a "B," or bypass, trust for the kids. He can put unlimited assets into the A trust and assets worth up to \$600,000 in the trust. (He could put in mo-



ESTATE PLANNING Trusts can elude estate taxes by enveloping assets in a kind of legal shrink-wrap

how funds are distributed. "This eliminates some concern over a child receiving a huge lump sum and wasting it," says John Donlon, advanced underwriting officer for the U.S. headquarters of Sun Life Assurance Co. of Canada in Wellesley, Mass.

It's best to set up a life-in-

payments using all or part of the \$10,000-a-year gift that could be given to each beneficiary tax-free.

Another irrevocable trust arrangement can help protect both a spouse and the children. A husband (or wife) can pass unlimited assets to a spouse tax-free, but then his

but would have to pay gift tax on the excess.) The wife could be trustee of and use principal and income from both trusts. Yet up to \$1.2 million can pass without estate tax to the kids.

A different irrevocable marital trust, useful for estate planning rather than tax avoidance, is the Q-tip, a qualified terminable interest property trust. Usually established in the will, the Q-tip lets you pass interest in your property to your spouse for

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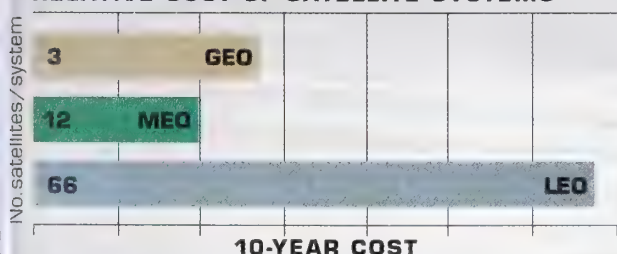
In a world in which most people lack access to even basic telephone service, this constellation of 12 medium-earth orbit satellites will provide

convenient, effective, consistent communications to subscribers around the globe. And it will do so at a price that compares favorably with the cellular service it will augment where such service exists, regardless of regional or carrier compatibility. Where terrestrial systems are absent, or when they are interrupted, your handset will link you directly – and transparently – to an Odyssey satellite.

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specify to whom it will revert upon your spouse's death. This could assure that if the husband dies and the wife remarries and has a second family, his children still get the asset.

A useful way to remove an expensive home from the estate is by locking in its lower value, before it appreciates, through a QPRT, or qualified personal residence trust. Say spouses in their mid-40s each cede their one-half interest in the \$600,000 family home to their children but retain the right to live there for 20 years. "The right to occupy the home for that long is probably equal to about two-thirds of the value," says David Gerson of Ernst & Young in New York, "so the gift is one-third," or \$200,000 in this example. The husband and wife both take \$100,000 from their \$600,000 pots. By the time the heirs receive the property, it could be worth a lot more, but no tax will be due. Catch: When the 20 years is up, the couple will have to pay market rent to their kids. Also, if either dies, the trust dissolves, and the house is back in the estate.

A QPRT is a type of gran-

A Look at Estate Taxes



tor-retained interest trust (GRIT) that can be used to benefit family members. Other GRITs, which can own securities as well as real property, benefit nonrelatives. The point is the same: to establish the tax basis now, when the value of sheltered assets is low, rather than at death.

If you have a very high-growth asset, such as insider's stock, a grantor-retained

annuity trust, or GRAT, can remove the future appreciation from your estate. To achieve any benefit, the asset has to grow more than the IRS's current discount rate of 9.4%. Say a person places securities worth \$1 million in the GRAT, agreeing to draw out a fixed amount each year for the next 20 years. The present value of this annuity arrangement is a mere \$43,500, according to IRS tables, which is applied against the \$600,000 exemption.

If you beat the tables, you could bequeath a bonus. After the annuity payments, a stock returning 13% a year on average would produce a trust worth \$485,000 in 20 years—more than a tenfold increase over the exemption amount. Withdrawals are mandatory. So if the asset returns less, you could draw out principal until the trust is depleted, and you're not better off than you were when you started—plus you've forfeited \$43,500 of your exemption and the

A Matter Of Trusts

LIFE-INSURANCE TRUST Shelters life-insurance proceeds from estate and income taxes; irrevocable; can't change beneficiaries; can't borrow against the policy.

A AND B TRUSTS Allow grantor to pass unlimited assets tax-free to spouse in an "A" marital trust while retaining a \$600,000 estate-tax exemption for other heirs in a "B" bypass trust; irrevocable.

Q-TIP (QUALIFIED TERMINABLE INTEREST PROPERTY TRUST) A planning—rather than tax-avoidance—vehicle that lets a husband or wife pass property to the surviving spouse and specify to whom it will go upon the spouse's death.

QPRT (QUALIFIED PERSONAL RESIDENCE TRUST) A way to remove a house from an estate and still retain the right to live in it for a set number of years; dissolves if you die before the trust term is up; you must pay market rent to stay put after the term expires.

CHARITABLE REMAINDER TRUST Lets you bequeath property to a charity, take an immediate tax deduction on its value, and use it or retain the income it produces while you live.

GRAT (GRANTOR-RETAINED ANNUITY TRUST) Lets you set aside money or securities, receive an annuity for a fixed number of years, and reduce the value of the gift to heirs for tax purposes; expensive to create; if you die prematurely, the GRAT reverts to your estate.

high cost of creating such a trust. GRATs of less than \$1 million are uneconomical.

One popular trust, used more for its current tax benefit than estate-tax purposes, is a charitable remainder trust. It allows you to bequeath property to a charity, take an immediate tax deduction, and use it or retain the income while you live. Say you have \$20 million worth of stock in a high-growth company, which pays little or no dividend. Put it into the trust and sell it, so you avoid capi-

tal-gains taxes, and invest the proceeds in something with high current income. "Now, I've got the whole \$20 million earning money for me," says Robert Lipsey, general counsel of Mid-Atlantic Cos., estate planners in Mt. Laurel, N.J.

FREEBIE. The maximum tax rate on trust income is the same as the top income-tax rate, but you get there quicker—currently, after just \$7,500. Unless you or your heirs need the cash, therefore, fund your trusts with growth assets, such as private undeveloped land and small-cap stocks.

As you plan, do not forget that you are also allowed to give anyone you choose an after-income-tax gift of up to \$10,000 each per year, on which the recipient pays no tax whatsoever.

Trusts can be intimidating but they aren't necessarily expensive to create: a few hundred dollars for the commonest types, up to perhaps \$20,000 for complicated plans. Uncle Sam could face a stiff tab, from the point of view of lost revenues. That could make your trust your last laugh. *Timothy Middleton*

WORTH NOTING

■ **WOMEN AND WEALTH.** Calvert Group in Bethesda, Md. is offering two free educational resources, *Investing Your Way: A Personal Economy and Investment Guide for Women* and *A Personal Economy and Financial Program for Women*. The booklets (800 SHE-INVESTS) offer women—who earn and save less but live longer than men—a primer on investment markets, a mutual-fund guide, asset-allocation tips, and other advice.

■ **VIRTUAL FISHING.** Until now, devoted trout fishers could only tie flies and tell lies during the long, cold off-season. But out of Silicon Valley comes *Fly Fishing: The McCloud River*, a compelling MS-DOS computer game. The user must pick the right fly and, using the mouse, land cybertrout as wily as the rainbows in the real McCloud, famed Northern California trout river. Through Orvis San Francisco (415 392-1600), \$49.95.



ASIA Now

How Asian Enterprise Is Transforming The Global Economy

THE 1994
BUSINESS WEEK
ASIA CHIEF EXECUTIVE FORUM



...rious expansion. Development-minded governments. Abundant labor. Extensive capital reserves. Burgeoning consumer markets. Asia is now the envy of the world, posting the highest rates of annual economic growth of any region, and poised for its role as the power sphere of the next century.

"The Asia-Pacific region in the past decade has scored an average annual growth rate of 6%—much higher than NAFTA's 2.7% and the EEA's (European Economic Area) 2.3%," says **Lee Teng-hui, President of Taiwan, R.O.C.** "Of the world's three economic blocs, the Asia-Pacific region has the greatest development potential—this should not be overlooked."

President Lee was joined by management guru Dr. Peter Drucker, Acer Inc. Chairman and CEO Stan Shih, Fuji Xerox Chairman and CEO Yotaro Kobayashi, and more than 100 chief executives from Asia's premier enterprises at The 1994 Business Week Asia Forum of Chief Executives in Taipei, Taiwan. The Forum was co-presented by *Business Week* and the Ministry of Economic Affairs, Taiwan, R.O.C.

And though overlooking Asian development is nearly impossible, *Asia Now* is but a promise; to make good on it, senior government and corporate chief executives must address the challenges of the development cycle and adapt their policies, management styles, and strategies accordingly.

RIDING THE WAVE

Asia's boom is no accident: a crescent wave swelling first in Japan and South Korea, breaking in coastal China, and reaching the shores of Southeast Asia. Over the past fifteen years, governments of the region have replaced import substitution policies with export promotion measures and supported industrial and commercial investment with major infrastructure development projects.

Add to that the sheer dynamism of the region—30.8% of the world's population, 20.7% of the world's GNP, plentiful natural resources, and high levels of saving—and the rising tide raises a powerful Asian fleet.

Moreover, the range of the region's economies has made Asia's development self-sustaining—as economies advance and wages rise in one country, less-developed neighbors benefit and the region grows and grows.

Vincent Siew, Chairman of Taiwan's Council for Economic Planning and Development says, "Export competitive-



ROBERT E. MITTELSTAEDT, JR.,
Vice Dean and Director,
The Wharton School of the
University of Pennsylvania

"We will all become more effective citizens of the global business community as we spend more time together in educational and business activities learning effective mechanisms for coping with problems that are very similar."



STAN SHIH, Chairman and Chief Executive Officer, Acer Inc.

"As a high-tech company from Taiwan, in order to gain global recognition, we must do much better than our competitors in the U.S., Japan, and Europe. We intend to achieve that through consistent quality and our unique management philosophy."

ticularly important. "We will all become more effective citizens of the global business community as we spend more time together in educational and business activities learning effective mechanisms for coping with problems that are very similar."

THE TECHNOLOGY IMPERATIVE

To acquire the technology needed to compete internationally, Haw Par Brothers' Hong suggests two strategies: use Asia's capital strength to buy into Western technology-based companies and tap into their innovative engineering; or forge strategic alliances with multinationals from advanced countries. In the latter arrangement, Western multinationals would supply technology and marketing channels in the West, while Asian multinationals would supply the local distribution networks and marketing know-how within Asia.

Almost twenty years ago Taiwan's Acer Inc. did just that, bringing U.S. technology to its home base in Taiwan. By 1982, Acer began manufacturing its own computers, and introduced its first PC in 1983. Today Acer competes head to head with its Japanese, American, and European rivals. But Acer has found that despite its industry-standard setting technology, establishing a global brand name as a non-Japanese Asian company is still a considerable challenge.

"Computers from the U.S. and consumer electronics from Japan are perceived worldwide as innovative. Computers from Taiwan still don't imply innovation, even though many computers are actually designed here," says **Acer Inc. Chairman and CEO Stan Shih**. To combat that perception problem Shih has created a three-tiered strategy.

Acer's "local-touch brand name" approach will create local shareholder majorities in each of its key markets, so that in each country the brand is perceived as domestic. Second, Acer's 'fast-food' business model has allowed it to assemble PCs in over 20 countries so it can deliver consistent quality as fast as domestic competitors. Third, the company is restructuring itself into 21 companies to keep each unit focused and create an entrepreneurial environment.

"Technology is a commodity," says Shih. "As a high-tech company from Taiwan, in order to gain global recognition, we have to do much better than our competitors in the U.S., Japan, and Europe.

We intend to achieve that through consistent quality and our unique management philosophy."

HARD CHOICES ON 'SOFT' ISSUES

The future for companies like Acer—companies that are addressing management and marketing challenges—is extremely bright. But Amnuay Viravan, founder of Thailand's new Leadership for Thai Party, and former deputy Prime Minister of Thailand cautions that the political dynamics must not be taken for granted.

Viravan identifies North and South Korea, China's territorial claims on Hong Kong-Taiwan-Shenzhen triad, and the fragile peace settlement in Cambodia as unresolved political conflicts that could explode and derail Asia from its route to prosperity. "The Asia-Pacific, with its ethnic, religious, and cultural diversity, is potentially very vulnerable. The most dangerous points seem to be located in archipelago Southeast Asia with its Islamic population and in China's peripheries."

Dr. Drucker warns that the explosion of development on mainland China will make it the world's most critical region for the next five to ten years. "It is certainly the most dangerous area economically speaking," Drucker warns that China's peasant population may be pushed to the limit, with a paucity of jobs on the land and no place for them in the economic boom of the coastal cities. "These will be the critical years in east Asia since the Maoist invasion. But with any luck, by the year 2005, China may also be the world's number two economic power. China is a question mark."

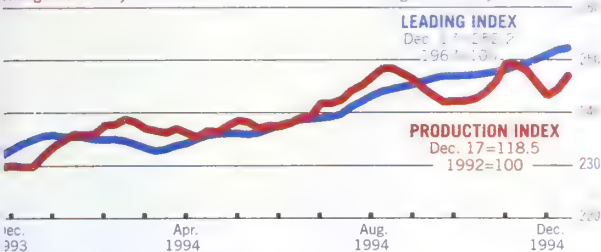
Martin A. Keohan
is a New York-based business writer.

Business Week Index

PRODUCTION AND LEADING INDEXES

Change from last week: 1.1%
Change from last year: 7.8%

Change from last week: 0.2%
Change from last year: 7.4%



production index increased during the week ended Dec. 17. Before calculating the 4-week moving average, the index also rose, to 121.5 from 118.5, led by strong increases in auto and truck output. leading index was up slightly in the latest week, but the unadjusted index fell to 118.5, from a revised 125.6. The drop reflected slower growth rates for materials prices and as well as an increase in business failures.

ADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (12/23) S&P 500	458.82	453.75	-1.6
CORPORATE BOND YIELD, Aaa (12/23)	8.45%	8.46%	21.6
INDUSTRIAL MATERIALS PRICES (12/23)	111.7	112.1r	NA*
BUSINESS FAILURES (12/16)	331	274	8.2
REAL ESTATE LOANS (12/14) billions	\$455.4	\$455.2	7.4
CREDIT SUPPLY, M2 (12/12) billions	\$3,559.0	\$3,598.3r	1.7
LEGAL CLAIMS, UNEMPLOYMENT (12/10) thous.	323	324	-1.5

Sources: Center for International Business Cycle Research (CIBCR), Standard & Poor's, Moody's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures of large companies), Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on business failures and real estate loans. *Historical data available from CIBCR

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
FEDERAL FUNDS (12/27)	5.60%	5.43%	2.99%
COMMERCIAL PAPER (12/28) 3-month	6.31	6.27	3.32
CERTIFICATES OF DEPOSIT (12/28) 3-month	6.37	6.22	3.24
FIXED RATE MORTGAGE (12/23) 30 year	9.34	9.41	7.29
ADJUSTABLE MORTGAGE (12/23) one year	6.73	6.83	4.28
RENTAL RATE (12/28)	8.50	8.50	6.00

Sources: Federal Reserve, HSH Associates, Reuters Holdings PLC

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (12/24) thous. of net tons	NA	1,988#	NA
AUTOS (12/24) units	141,940	149,575r#	22.1
TRUCKS (12/24) units	110,958	119,379r#	16.0
ELECTRIC POWER (12/24) millions of kilowatt-hrs.	NA	62,279#	NA
CRUDE-OIL REFINING (12/24) thous. of bbl./day	NA	13,905#	NA
COAL (12/17) thous. of net tons	20,504#	21,413	11.7
PAPERBOARD (12/17) thous. of tons	858.8#	827.0r	0.1
PAPER (12/17) thous. of tons	817.0#	823.0	2.9
LUMBER (12/17) millions of ft.	499.7#	483.2	3.9
RAIL FREIGHT (12/17) billions of ton-miles	24.5#	25.4	6.5

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPAA, SFPAA, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (12/28) \$/troy oz.	381.750	382.050	-1.1
STEEL SCRAP (12/27) #1 heavy, \$/ton	143.50	143.50	2.9
COPPER (12/24) ¢/lb.	140.4	140.8	64.5
ALUMINUM (12/24) ¢/lb.	91.0	89.0	71.7
COTTON (12/24) strict low middling 1-1/16 in., ¢/lb.	82.14	80.74	34.7
OIL (12/27) \$/bbl.	17.64	16.98	24.2

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (12/28)	100.32	100.22	111.68
GERMAN MARK (12/28)	1.57	1.57	1.74
BRITISH POUND (12/28)	1.54	1.56	1.48
FRENCH FRANC (12/28)	5.43	5.43	5.89
ITALIAN LIRA (12/28)	1642.8	1643.5	1712.6
CANADIAN DOLLAR (12/28)	1.40	1.39	1.33
MEXICAN PESO (12/28) ¹	4.975	3.975	3.106

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

SURVEY

Monday, Jan. 3, 10 a.m. ► The National Association of Purchasing Management's index probably declined a bit in December, to 61.2%, down from 61.2% in November. The median forecast of economists released by MMS International, a division of Law-Hill Inc. November's NAPM reading, the highest in 10 years, was led by a steep increase in the purchasers' production index.

CONSTRUCTION SPENDING

Tuesday, Jan. 4, 8:30 a.m. ► Warm weather in November probably lifted building starts by a modest 0.5%, say the MMS economists. That's suggested by the 7% increase in the month's housing starts. Despite

higher interest rates, the construction industry has been holding its own: Spending grew 1.7% in September and 1% in October.

FACTORY INVENTORIES

Thursday, Jan. 5, 10 a.m. ► Inventories held by manufacturers probably grew by about 0.5% in November. If so, that would be the seventh advance in the past eight months. In October, inventories increased by 0.4%.

VEHICLE SALES

Thursday, Jan. 5 ► Sales of U.S.-made cars and light trucks likely slipped a bit in December, to a combined annual rate of 13.5 million, down from November's pace of

nearly 14 million. The MMS economists project that the buying weakness is concentrated in light trucks, with sales probably falling to 6.1 million in December, down from 6.6 million in November.

EMPLOYMENT

Friday, Jan. 6, 8:30 a.m. ► The MMS survey projects that nonfarm payrolls increased by 260,000 workers in December, on top of November's 350,000 new hires. That would mean 3.85 million jobs were created in 1994. Manufacturing jobs probably rose 30,000 in December, after increasing by 51,000 in November. The jobless rate at the end of the year is expected to be 5.6%, the same reading as in November.

Index to Companies

This index gives the starting page for a story or feature with a significant reference to a company. Most subsidiaries are indexed under their own names. Companies listed only in tables are not included.

A

ABC 6
Adobe 120
Advanced Micro Devices 77, 106
Aetna Life & Casualty 94
AK Steel 68, 108
Alex. Brown & Sons 77
Allegro New Media 22
Alvey 65
A.M. Best 94
American Airlines 88
American Iron & Steel 68
America Online 76, 115
Amgen 79
Amoco 81
Andersen Consulting 88
Annex Research 75
Apache 81
Apple Computer 42, 54, 77, 110, 117, 120
Applebee's International 89
Applied Materials 77
Archer Daniels Midland 49, 72
Arthur Andersen 63
AT&T 15, 54, 76, 78
ATX 47
Autofacts International 54
AutoPacific 41

B

Baring Securities 34
Barriett Banks 93
Bearings 87
Bear Stearns 54, 69, 81, 90
Bell Atlantic 78
BellSouth 51
Berkeley Systems 42
Bertucci's 89
Bezeq
Telecommunications 51
Birmingham Steel 68
Blockbuster Entertainment 108
Boeing 14E1
Boise Cascade 83
Borden 72
Borland International 22
Bose 114
Brinker International 89
Bristol-Myers Squibb 79
British Petroleum 81
British Steel 68
Broadview Associates 76

C

Cadbury-Schweppes 6
Caesars World 47
Calvert Group 122E4
Campbell Soup 72
Cancer BioScience 36
Capital Cities/ABC 91
Cardinal Health 87
CBS 8, 91
C-Cube Microsystems 77
CellCom 51
Cementos Mexicanos 34
Chaparral Steel 68
Chase Manhattan 93
Checkers Drive-In Restaurants 89
Chemical Banking 93
Chicago Corp. 89
Chiron 79
Chrysler 8, 63, 106, 118
Chubb 94
CIGNA
Cincinnati Milacron 65
Cirrus Logic 77
Citibank 93

Coca-Cola 8, 104

Coleman 40
Columbia/HCA Healthcare 85
Columbia Sportswear 104
Commonwealth Edison 90
Compaq Computer 54, 75, 110, 120
CompuServe 76, 115, 120
ConAgra 49, 72
Consolidated Engineering 13
Continental 94
Continental Airlines 8, 88
Cooper Industries 40
Corporate Software 120
Cowen 79
CPC International 72
Cramer Rosenthal McGlynn 47
Cray Research 47
Creative Labs 120
CRSS 122
CS First Boston 93, 122
Cushman & Wakefield 98
Cypress Semiconductor 77
Cyrix 77

D

Dataquest 75, 76, 77
Dean Foods 72
Dean Witter Reynolds 83
Dell Computer 54, 120
Deloitte & Touche 54
Delrina 120
Delta Air Lines 88
Denny's 89
Deutsche Bank North America 47
Digital Equipment 120
Dime Savings Bank 105
Discount Investment 51
Diversified Pharmaceutical Services 87
Domino's Pizza 89
Donaldson, Lufkin & Jenrette 85
Dow Chemical 79
Dr Pepper/Seven-Up 6
DRI/McGraw-Hill 54
DuPont 54, 69

E

Eastman Kodak 79, 105
Eaton 63
Ebasco 122
Eddie Bauer 86
Electronic Arts 91
Electronic Data Systems 6
Elektra Entertainment 106
Eli Lilly 87
Enserch 122
Equitable Real Estate Investment Management 98
Ernst & Young 93, 122E2
E-Systems 64
Exxon 81

F

Federated Department Stores 86, 110
Fidelity Investments 6, 95
First Alert 44
Fleet Financing 93
Fluor 122
Foamex International 69
Ford 41, 54, 63, 105, 108, 118, 119
Forrester Research 42
Foster Wheeler 122
Fox 46, 47, 91
Fresh Choice 89
Fuji Electric 51

G

Gallatin Steel 68
Gap 86
Gardener's Eden 86
Gardner Denver Machinery 65
Gartner Group 75
Gateway 2000 22, 120
GE 8, 91, 122
General Dynamics 64
General Magic 119
General Mills 72
Gerber 72
GM 54, 63, 105, 119
Goldman Sachs 30, 54, 106
Green Gear Cycling 118

H

Harris 64
HCIA 85
HealthTrust 85
Heinz (H.J.) 72
Hewlett-Packard 75, 77, 118, 120
Hillhaven 85
Hitachi Electronics 51
Honda 41
Hughes Aircraft 64
Hughes Electronics 6

I

IBM 15, 54, 75, 77, 104, 110, 117, 120
IBP 72
Industrias Penoles 34
Inland Steel 68
Intel 6, 77, 104, 106
InterMedia Partners 91
International Data 75
Intuit 76, 106, 112
ITT 8, 47, 64, 65
Ivax 36

J

Jacobs Engineering 122
Jaguar 63
J.C. Penney 86
J.D. Power & Associates 106
John Hancock Mutual Life 94
J.P. Morgan 63, 93

K

Kellogg 72
Kent Laboratories 13
Kidder Peabody 8, 78, 95
Kmart 86
Knowledge Adventure 112
Kohlberg Kravis Roberts 8
KPMG Peat Marwick 79
Kurt Salmon Associates 86

L

Ladenburg Thalmann 122
Lehman Brothers 54, 98, 122
Ligand Pharmaceuticals 36
LINC Group 85
Lipper Analytical Services 95
Little Caesar Enterprises 89
L.L. Bean 115
Lockheed 64
Longview Fibre 83
Lotus Development 76, 166, 120
Louisiana-Pacific 83
LSI Logic 77
LTV 68
Luntz Research 40

M

MacAndrews & Forbes 40
Macy (R.H.) 86, 110
Madison Square Garden Corp. 108
Management Horizons 86
Marion Merrell Dow 79
Mars 47
Martin Marietta 64
MasterCard International 31
Matsushita 103
MCA 103
McCann-Erickson Worldwide 91
McCaw Cellular 78
McDonald's 89, 102
McDonnell Douglas 64
McGraw-Hill 127
MCI 78
McKinsey 81
Mead 83
Meadow Gold Dairies 72
Medco Containment Services 87, 102
Medical Care America 85
Medtronic 85
Megatest 77
Meidensha 51
Merck 8, 79, 87, 102
Merrill Lynch 30, 54, 78, 81, 95, 100
Merry-Go-Round 47
Mesa 47
Metropolitan Life 94
Micron 120
Microsoft 6, 22, 36, 42, 75, 76, 91, 106, 112, 119, 120
Mid-Atlantic 122E2
Milliman & Robertson 85
Mitsubishi Caterpillar Forklift America 65
Mitsubishi Electric 51
MMS International 127
Mobil 81
Monsanto 40
Moody's Investors Service 88
Morgan Stanley 30, 34, 75, 95
Motorola 8, 51, 77, 90, 102, 105, 114, 117

N

NACCO Materials Handling Group 65
National Bank of Canada 34
NationsBanks 93
NatWest Securities 38
NBC 46, 91
Nektan Pilot 117
Nestlé 72
Netscape Communications 112
News Corp. 46
NFL 91
Nikon 116
Nintendo 108, 117
Nokia 102, 116
Northgate 120
Northrop Grumman 64
Northwest Airlines 88
Norwest 47
Novell 76, 112, 120
Nucor 68
Nynex 78

O

Oakmark International 47
Office Depot 87
OfficeMax 87
Oldsmobile 114
Oppenheimer 46, 91
Oracle 36, 76
Orvis 122E4

Outback Steakhouse 89

Oxford Health Systems 85
Pacific Gas & Electric 90
Pacific Telesis 78
Packard Bell 114, 120
PaineWebber 8, 68, 95
Paramount 46, 47, 108
Patagonia 104
Pathfinder Research 77
PCS Health Systems 87
PCCS Energy 90
Pennzoil 81
PepsiCo 89
Pet 72
Pfizer 79
Pier 1 Imports 86
Piper Jaffray 89
Pitt-Des Moines 122
Pizza Hut Worldwide 89
Plum Creek Timber 83
PNC Financial 93
Pollo Tropical 89
Polycorn 22
Pottery Barn 86
Price Waterhouse 38
Pro CD 22
Prodigy 115
Provident Life & Accident 94
Prudential Insurance 8, 94

Q

Quaker Oats 72
QVC 8

R

Ralcorp Holdings 72
Raytheon 122
Regional Financial Associates 54
Reliance Electric 64, 104
Reno Air 88
Rhône-Poulenc Rorer 79
RJR Nabisco 72
Robert Morris Associates 93
Roche Holding 79
Rockwell International 64, 104
Royal Dutch/Shell 81

S

Saatchi & Saatchi 47
Salomon Brothers 34, 54, 63, 79, 94
Sandoz 8, 36
Sanford C. Bernstein 85
Sara Lee 72
SBC Communications 78
Schering-Plough 79
Sears 8, 40, 86
Seiko 115
SGS-Thomson 77
Silicon Graphics 108, 112, 117
Smith Barney 122
SmithKline Beecham 79, 87
Snapple 72
Softbank 112
Somatix Therapy 36
Sony 116, 119
Southwest Airlines 88
Spiegel 86
Sprint 78
Standard & Poor's 115
Stationers Distributing 87
Sterling Winthrop 79
Sumitomo 68

Sun Life Assurance 122E

Sun Microsystems 75
SuperValu 87
Sybase 76
Symantec 120
Synergen 79
Syntex 79
Taco Cabana 89
Talbott 86
Tandy 86
Taylor Made Golf 115
Technomic 89
Tektronix 110
Tele-Communications 9
Teledyne 47
Teléfonos de México 34
Tenneco 64
Texaco 81
Texas Instruments 64, 7
The Limited 86
Thomson Consumer Electronics 118
Tiffany 86
Time Warner 46, 105, 110
TLC Beatrice 105
Toronto Blue Jays 114
Toshiba 51
Toyota 41, 114
Toys 'R' Us 47
Travelers 94
Tribune 46
Triton Energy 81
Tyson Foods 72

U

Unilever 72
Union Carbide 69, 122
United Airlines 14E1, 8
United HealthCare 85
United Paramount Network 46
United Stationers 87
UNUM Life Insurance
Upjohn 47
USAir 88
U.S. Steel 108
U.S. Trust 93
U S West 78

V

ValuJet 88
Veronis, Suhler & Associates 91
Viacom 46, 91, 108
Visa 31
VLSI Research 77

W

Wal-Mart Stores 86
Walt Disney 6, 91, 104, 120
Warner-Lambert 79
WB Network 46
Weight Watchers 72
Western Atlas 65
Western Resources 90
Westinghouse Electric
Wetterau 87
Weyerhaeuser 83
WGN 46
WHX 47
Williams-Sonoma 86
World Class Processing 112
W.R. Grace 69

Z

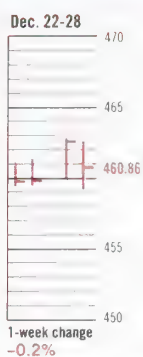
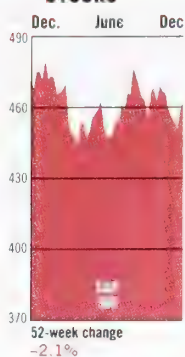
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Investment Figures of the Week

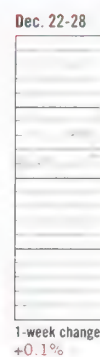
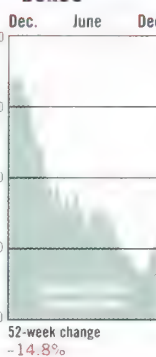
MENTARY

Week in the world financial markets, which were rocked by the peso after the Mexican government abandoned its policy of supporting the currency. Bonds took a big hit on Dec. 28, the largest drop since Nov. 1, as a result of concern that investors may be pulling out their portfolios to make up for losses from the peso. Yield of 30-year Treasury bonds rose to 7.8%. U.S. stocks fell on Dec. 28, ending a four-day rally. Retail stocks led the list of losers.

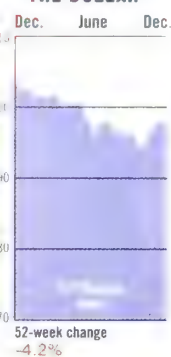
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	% change	
		Week	52-week
DOW JONES INDUSTRIALS	3839.5	1.0	1.2
S&P 500 COMPANIES (S&P MidCap Index)	168.3	0.4	-5.3
S&P 500 COMPANIES (Russell 2000)	245.3	0.8	-3.3
S&P 500 COMPANIES (Russell 3000)	263.3	0.3	-2.9
INTERNATIONAL STOCKS	Latest	% change (local currency)	
		Week	52-week
DOW JONES FINANCIAL TIMES 100	3095.8	0.8	-9.3
NIKKEI INDEX	19,665.5	1.7	14.8
DOW JONES TO (TSE COMPOSITE)	4201.5	0.6	-2.0

FUNDAMENTALS

	Latest	Week Ago	Year ago
90-DAY TREASURY BILL YIELD	5.59%	5.54%	3.12%
30-YEAR TREASURY BOND YIELD	7.83%	7.84%	6.24%
S&P 500 DIVIDEND YIELD	2.79%	2.80%	2.36%
S&P 500 PRICE/EARNINGS RATIO	17.0	17.0	23.1
TECHNICAL INDICATORS			
	Latest	Week ago	Reading
S&P 500 200-day moving average	457.8	457.9	Positive
Stocks above 200-day moving average	31.0%	29.0%	Positive
Speculative sentiment: Put/call ratio	0.60	0.66	Neutral
Insider sentiment: Vickers sell/buy ratio	1.07	1.17	Positive

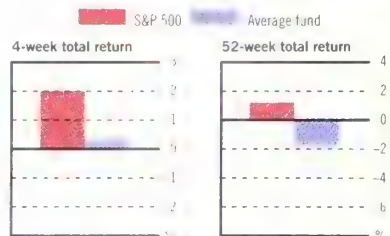
BLOOMBERG FINANCIAL MARKETS

INDUSTRY GROUPS

WEEK LEADERS	% change		Strongest stock in group	% change		Price
	4-week	52-week		4-week	52-week	
REBUILDING	16.9	-42.2	PULTE	23.3	-34.6	23 1/8
PACKAGING	13.9	-8.0	YELLOW	24.5	-6.0	23 1/2
TELECOM	12.4	37.8	NIKE	20.1	66.2	76 1/4
PROPERTY-CASUALTY INSURERS	10.9	3.9	CONTINENTAL	33.6	-32.9	18 7/8
PHARMACEUTICALS	10.1	15.2	ASARCO	12.6	36.3	29 1/8
WEEK LAGGARDS	% change		Weakest stock in group	% change		Price
	4-week	52-week		4-week	52-week	
RETAIL APPAREL RETAILERS	-9.8	-17.8	GAP	-18.5	-28.5	29 1/8
GENERAL MERCHANDISE CHAINS	-9.4	-17.7	DAYTON HUDSON	-12.1	3.4	68 3/4
DEPARTMENT STORES	-8.9	-15.0	J.C. PENNEY	-11.9	-20.5	42 3/4
OIL AND GAS DRILLING	-8.0	-17.1	HELMERICH & PAYNE	-8.4	-7.6	25 3/4
TEXTILE MANUFACTURING	-5.9	-1.1	LIZ CLAIBORNE	-30.0	-25.0	15 1/4

MUTUAL FUNDS

LEADERS	Week total return	%	LAGGARDS	Four-week total return	%
STONE ISLAND AMERICA HARTWELL EMERG. GR. A	11.0		WRIGHT EQUIFUND-MEXICO NATL.FID.EQTY.	-31.5	
REAL ESTATE SECURITIES	8.7		FIDELITY LATIN AMERICA	-17.7	
MEXICAN CAPITAL REAL ESTATE SECS. A	8.7		TCW/DW LATIN AMERICAN GROWTH	-15.6	
Laggards	Week total return	%	52-week total return	%	
GLOBAL COMMUNICATIONS & INFORM. A	37.6		MONITREND GOLD	-50.7	
TECH SMALLER COMPANIES	28.4		STEADMAN OCEANOGRAPHIC TECHNOLOGY	-36.7	
BIOTECHNOLOGY A	28.4		STEADMAN AMERICAN INDUSTRY	-35.5	



DRUMMcRAW-HILL

ACTIVE PORTFOLIOS

Amounts represent the value of \$10,000 one year ago portfolio

Figures indicate percentage total returns

Foreign stocks
\$11,239
+1.07%

Money market fund
\$10,481
+0.32%

U.S. stocks
\$10,100
+1.00%

Gold
\$9,675
+0.25%

Treasury bonds
\$9,028
+1.16%

Figures on this page are as of market close Wednesday, Dec. 28, 1994, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are

as of market close Dec. 27. Mutual fund returns are as of Dec. 23. Relative portfolios are valued as of Dec. 27. A more detailed explanation of this page is available on request. r=revised.

INVESTMENT IS STILL A CAPITAL IDEA

The most striking economic phenomenon of the 1990s has been Corporate America's investment juggernaut. Battered by international competition, companies across the U.S. regrouped in the late 1970s and 1980s. They slashed costs, stressed quality, and streamlined bureaucracies. By the 1990s, they began the biggest investment boom in decades, pouring billions of dollars into new computers, telecommunications gear, software, and other capital equipment. The payoff: stronger growth, higher productivity, and record profits.

Now, 1995 is shaping up as the year when the long-anticipated slowdown in the economy finally materializes. The consensus among economists is that aggressive tightening by the Federal Reserve Board last year and expected interest-rate hikes early this year will slow the economy's growth rate to 2.5% or so, down sharply from the 3.5% average gain of the past two years. A reading of this week's *Industry Outlook* suggests companies are a bit more optimistic (page 54).

Whether the economy throttles down a bit or a lot, it's vital that the investment boom rolls on. Sure, it's hard for any chief executive to sink shareholder money into a risky new plant or computer system when consumer demand is becoming more uncertain. Yet high levels of investment spending are a simple necessity in a global economy. U.S. companies and their workers will continue the battle for profits and market share against a resurgent Japan and Europe as well as the vibrant economies of the developing world, from Malaysia to Argentina. More capital equipment behind each U.S. worker means more productivity, the basis of real economic wealth.

Public investment is needed as well for growth. Good roads and airports cut the cost of doing business. Good schools provide critical human capital. Wiring the nation's schools with fiber-optic cable could enhance our long-run competitiveness.

Investment isn't just bricks and motors, bits and bytes. It represents the appetite for risk that drives growth. When companies and nations invest, they're betting on new ideas, new opportunities, new horizons. These bets have paid off big so far in the 1990s. They will into the millennium.

A BETTER WAY TO PAY FOR COLLEGE

For families straining to send their children to college, President Clinton's recent college-tuition tax-break proposal was an unexpected present. But taxpayers, as usual, should beware of federal officials bearing gifts.

For starters, the tax break could allow college administrators to avoid necessary cost-cutting. College costs have shot into the stratosphere—growing at more than double the rate of inflation. Tuition costs have swelled largely because of

bloated educational bureaucracies, the product of campus politics that prevents cuts in both administrative personnel and weak academic departments. Only recently have some universities begun to embrace reforms made by many corporations: zero-sum budgeting, decentralization, automation outsourcing of back-office functions, and focusing on what they do best. Chances are college administrators will use Clinton's plan as a license to continue raising tuition to avoid painful restructurings.

That, of course, would be inflationary. Between the end of 1977 and 1994, college tuition has shot up 347%, compared with 265% for medical costs and 141% for the consumer price index. Astounding!

Far better than a convoluted tax-deduction scheme would be for the President to simply cut the marginal tax rates for all middle-class families and allow them to retain more of their earnings. That would help families pay for college without encouraging administrators to boost tuition. The President should then cut government spending on middle-class entitlements by a like amount to pay for the tax cut.

Much of academe, like Corporate America during the 1970s, has become inefficient, unproductive, and uncompetitive. The current Clinton proposal, despite its good intentions, would only perpetuate that disturbing trend. He can do better.

THE PESO'S PLIGHT—IN PERSPECTIVE

It's time for investors to look beyond the hysteria over Mexico's currency crisis. Despite a frightful drop that sent the peso plummeting more than 30% against the dollar, Mexico remains a promising market for investment. And U.S. companies—and investors—would be wise to keep the pain born of government miscues in perspective.

Think about it. Mexico has an independent central bank, a low budget deficit, and an ongoing commitment to privatize state-owned industries. It has an enormous asset in the emerging global economy: unfettered access to the U.S. market, thanks to the North American Free Trade Agreement. Best of all, NAFTA provides clear, concise rules governing foreign investment that businesspeople would kill for in other booming Asian and Latin American countries.

This does not diminish the fact that the new government under Ernesto Zedillo Ponce de León has badly bungled the peso devaluation. A relatively strong peso has been the cornerstone of Mexico's anti-inflation policy for the past several years. Peso stability has been critical to encouraging foreign capital. Neither Zedillo nor Finance Minister Jaime Serra Puche prepared the markets for a major change in policy. They didn't provide information to creditors beforehand or come up with a financial package to restore confidence once the devaluation got out of hand. Both are now required. Zedillo's team must get its act together, or the President should bring in more financially sophisticated players. Mexico's future is too bright to be lost through lack of leadership.

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Lufthansa could have called on any bank to help them further privatize in October, 1994. But then, Lufthansa doesn't like turbulence. So they called their preferred "Tower" to arrange and lead the deal: Dresdner Bank.

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Dresdner Bank
for guidance.

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PEOPLE THE EDUCATION OF ANDY GROVE CONGRESS HOW WILL BUSINESS FARE? STRATEGIES APPLE TOSHIBA SEAGRAM

BUSINESS WEEK

95 January 16

BusinessWeek

JANUARY 16, 1995

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MEXICO CAN IT COPE?

Zedillo's plan
means plenty
of pain ahead

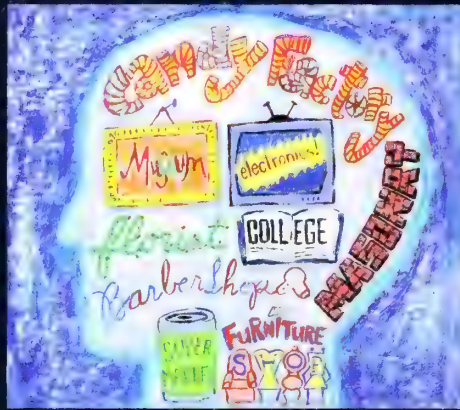


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BusinessWeek

JANUARY 16, 1995

COVER STORY

Mexico's peso crisis will stunt its growth—and Zedillo's disappointing recovery plan only makes matters worse

page 42

Cover Story

42 MEXICO: CAN IT COPE?

The peso shock demanded strong leadership, but so far, President Zedillo's political moves have been bumbling, and his rescue scheme seems timid. Mexicans, foreign investors, and the Clinton Administration are all wondering how to pick up the pieces

47 TIGHTLY HITCHED

Like it or not, the U.S. can't afford to let its neighbor crumble

48 CURRENCIES ON THE EDGE

Many economists think 1995 could see debt and money crises across the world

55 BARGAIN-HUNTERS, LOCK AND LOAD

For those of stout heart, Mexican stocks will become ever-easier prey

News: Analysis & Commentary

28 MAIN ST. VS. CORPORATE AMERICA

Under Washington's probusiness banner are two distinct camps

9 HASTA LA VISTA, WELFARE MOM?

Both Clinton and the GOP are talking tough—but their benefit cuts vary a lot

31 A SURPRISE SQUEEZE PLAY

The GOP takes aim at the baseball owners' antitrust exemption

32 WHY NOT CALL THEM 'SCAMMERS'?

Investigators say electronic checkout systems frequently overcharge

33 COMMENTARY

The minority set-aside for broadcast licenses is a loophole big enough for a media mogul to waltz through

34 IS ITT ROLLING THE RIGHT DICE?

Caesars Palace may not give ITT the easy entry into the gaming business that it's looking for

35 GOODYEAR'S GAULT HAS A FLAT TO FIX

The tiremaker's CEO is trying to buff up his legacy before he retires at the end of the year

36 A HEALTH KICK AT WEIGHT WATCHERS

Boss David Sculley is zeroing in on dieters' physical well-being with a health-before-vanity message

37 NOT YOUR GRANDMA'S GIRDLES

They're called "body smoothers"—lightweight lingerie that provides support for today's sagging boomer

38 IIN BUSINESS THIS WEEK

Kraft foods, CBS and Tisch, Tandy, the 3¢ stamp, Caremark, Coke vs. seltzer, Legent's new CEO

Government

41 WASHINGTON OUTLOOK

The GOP takes a hard look at deriving a job on the Job Corps

International Business

59 INTERNATIONAL OUTLOOK

Who's pulling the Kremlin's strings

Economic Analysis

20 ECONOMIC VIEWPOINT

Dornbusch: Blame Salinas for the p

24 ECONOMIC TRENDS

Computers as a spur to output, ske data on GDP and imports, a credit-c conundrum, the buck's buying powe

25 BUSINESS OUTLOOK

Why many businesses could feel cheated this year

76 WHAT'S THE YIELD CURVE SAYING?

Economists can't agree on its signa



THE RUMPUS START!
Congress gets under way, all and big business jostle position page 28



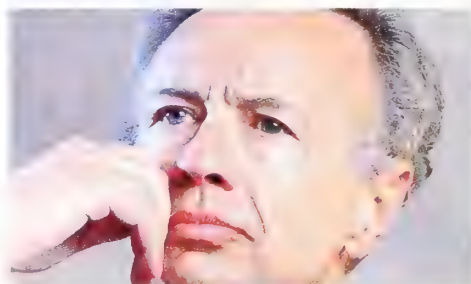
MACYEAR?
Apple is in fighting trim, and its licensing chief is starting to sign up clone makers page 84



EDGAR'S EFFORTS
At Seagram, many of Edgar Bronfman Jr.'s big moves—from Tropicana to Time Warner—have been slow to pay off page 78



BUYING STOCKS LIKE CLOCKWORK
Automatic investment plans offer a smart way to build a solid portfolio page 92



ANDY'S ANSWER
Intel's chief insists the chipmaker isn't in need of a cultural revolution page 60

People

THE EDUCATION OF ANDY GROVE

As the Pentium mess shows, Intel's feisty CEO is still learning how to market to consumers

Finance

MELLON-CHOLY BABY

Initially heralded as a dream deal, the Mellon-Dreyfus merger has encountered some snags

INSURERS: LOOKS LIKE A SEA CHANGE

After an eight-year slump, the property-and-casualty industry cycles may be a thing of the past

THE PHANTOM OF ORANGE COUNTY

As the SEC sifts through the rubble, little-noticed financial adviser Jeffrey Leifer is suddenly on the hot seat

INSIDE WALL STREET

Ron Perelman: Las Vegas or bust? Equifax eyeballs medical records What may heal Organogenesis

INVESTMENT FIGURES OF THE WEEK

The Corporation

78 BIG SPENDER AT SEAGRAM

Edgar Bronfman Jr. is pushing the spirits giant beyond its core business, but some say his buys are too pricey

Science & Technology

80 DEVELOPMENTS TO WATCH

Value-free software, a supercollider for CERN, robosuits, edible cotton

81 THE FAIREST OF THE FAIRS

ISEF science fairs draw the whiz kids—and U.S. business is starting to notice

Legal Affairs

82 THE ASBESTOS CASE OF THE 1990s?

Injured typists vs. keyboard makers

Information Processing

16 TECHNOLOGY & YOU

Pagers that can spell it all out

84 APPLE IS LOOKING RIPE

The computer maker is geared up to boost market share and profits

86 TOSHIBA: ON TOP IN LAPTOPS

Once caught napping, it's back on track

Sports Business

91 THE NBA'S FASTEST FIVE-FOOTER

Washington Bullets President Susan O'Malley knows how to draw a crowd—even with a lackluster team. Now she's getting a spanking new arena

Personal Business

- 92 INVESTING:** Stocks on autopilot
SMART MONEY: Long-term bonds
HEALTH: Oxygen therapy

Features

4 UP FRONT

10 EDITOR'S MEMO

11 READERS REPORT

15 BOOKS

Clifford: *Troubled Tiger: Businessmen, Bureaucrats, and Generals in South Korea*

99 BUSINESS WEEK INDEX

100 INDEX TO COMPANIES

102 EDITORIALS

Mexico still has a lot going for it
To cut welfare, cut the need for it

Up Front

EDITED BY LARRY LIGHT

NEWTONIAN ECONOMICS

TAX BREAKS: RICH FOLK FIRST

HOUSE REPUBLICANS HAVE vowed to cut taxes by \$200 billion over the next five years, but most Americans probably won't see the payoff before 1996. Relief will go first to investors with capital gains and to small businesses that write off equipment.



TAKING THE PLEDGE: *Already broken?*

BUSINESS WEEK has learned that House GOP leaders plan to postpone the effective date of middle-class tax cuts, because they couldn't find \$15 billion in offsetting spending cuts needed this year. The decision will delay such "pro

family" measures as a \$500 per child credit.

On the other hand, the leadership will try to index capital gains for inflation and cut the top rate to 14% from 28% for assets sold after Jan. 1, 1995. That date also would apply to more generous first-year write-offs for small business investment and new depreciation rules for capital purchases.

Leaders fear that postponing the changes would prompt companies and investors to delay investments until taxes drop. An immediate capital-gains cut also would pull in revenue in 1995 because people would be quicker to take profits on stock and other investments.

The GOP math shows the investment breaks generate a net gain of \$4 billion.

The rationale of Republicans might be good economics, but you can probably expect "party of the rich" rhetoric from the Democrats. *Howard Gleckman*

HONCHOS

THE CANONIZATION OF REGINALD LEWIS

THE LATE REGINALD LEWIS IS getting the full icon treatment. One of America's most celebrated black businessmen, Lewis, the subject of a recently issued biography, *Why Should White Guys Have All the Fun?*, had a building at alma mater Harvard Law School named after him, and a wax figure of him is on museum display in his hometown, Baltimore. Then there's his office at TLC Beatrice, the food outfit he bought in 1987. The room has been preserved as he left it, and schoolchildren tour it.

The commemoration of Lewis, who died at 50 in 1993 of brain cancer, has the altruistic purpose of inspiring young blacks. But it also is a powerful image-making tool



IN WAX: *Also in print*

TALK SHOW "Take your chairman into a corner and shoot him quickly—we don't want the fuss of a public trial."

—Maurice Saatchi, in a letter to Saatchi & Saatchi employees about the method of his removal as chairman

NEW WORLD ORDER

AN INFIDEL INVESTOR AMONG THE MULLAHS



SATAN'S ANGEL: *Rogers*

IRAN ISN'T A POPULAR emerging market. But at least one money man from the Great Satan is braving the Islamic republic's bourse. James Rogers, former partner of investing wizard George Soros, says he has bought shares in Iran's 10 largest companies on the tiny (market cap: \$1.7 billion) Tehran Stock Exchange.

Rogers, author of *Investment Biker*, a book about his motorcycle tours in search of investments, took a year to find an Iranian investment banker who would deal with him and started investing a year ago. "No one was executed," he says, so he has kept buying. Rogers, who

for Beatrice, which needs one. It has stumbled badly since the well-regarded Lewis' death, say analysts. Last year, investor pressure led to the resignation of Lewis' successor as chairman, his brother Jean Fugett, who couldn't be reached for comment. Minority shareholders—the Lewis family owns 55%—have sued to recover what they see as excessive compensation for Lewis. The new chairman, widow Loida Lewis, has been selling off some company units. While Beatrice, its business mainly in Europe, reported a strong third quarter (up 29% over the year-prior period), Wall Street is still skeptical. □

hasn't been to Iran, won't disclose the amount. His stocks include shares in a food processor, an auto parts maker, and a cement company.

Thus far, his timing has been deft. The Tepix index, the Persian equivalent of the Dow, surged 45% last year. Rogers says that's due to optimism that Iran will soon open to outsiders. Another factor may be a recent Iranian ban on currency trading, in effect restricting its investors to domestic stocks. □

FEE MANIA

AN OFFER MAYBE YOU SHOULD REFUSE

BANK CREDIT CARDS TOO steep for you? Wells Fargo just introduced a service that offers its customers a pay advance—and charges up to a hair-raising 60% annual rate for the privilege. Customers using direct deposit can get \$20 to \$200 up to a month ahead of their next paycheck. Tapping an automatic teller machine or calling a 24-hour phone line immediately lands the advance in their checking accounts. Pay-up time comes when the next electronic paycheck arrives at Wells.



WELLS FARGO & COMPANY

Banks everywhere are turning to fees for such services as check overdrafts, but Wells has proven more aggressive than most. For pay advances, its fee is \$1 for each \$20 increment borrowed. If charged as interest for a year, it would work out to an astounding 60% rate. Wells, the nation's seventh-largest bank, says any dissatisfied folks can get a refund on the fee. *Russell Mitchell*



Now.

Up Front

TRADING PLACES

A NEW WAY TO HOLD YOUR BEER

BEER CONNOISSEURS LOVE TO quaff gourmet suds from the microbreweries popping up in odd corners of the land. So the small-time brewers now hope to do at least as well



MICROBARONS: Brooklyn brewers

with stock in their companies. Microbreweries such as Portland Brewing in Oregon, Spring Street Brewing in New York City, and Mendocino Brewing in Hopland, Calif., have gone public in the

past year. Many more, such as Brooklyn Brewery, plan to do so soon. While pint-size breweries make up just 1% of the U.S. beer market, analysts expect that number to hit 10% in the next 10 years.

A warning: It's not easy to invest. None of these IPOs is large enough to be on any public exchanges. The companies are selling the shares directly, without benefit of an underwriter, and no brokers handle later trading.

Even if the microbrewing industry takes off, it may be like computers a decade ago: The small outfit you choose may not be the one to prosper. In the short term, don't look for dividends or price growth for these very thinly traded issues.

"It's pretty airy stuff," Tom Pirko, president of BevMark International, a beverage industry consultant, says. One plus for Portland Brewing shareholders: a free cold one if you visit. *Julie Tilsner*

I-WAY PATROL

WHAT'S A NICE COMPANY LIKE YOU...

AS THE PHONE COMPANIES move into a deregulated world, they're confronting the good, the bad, and the smutty. The latest? A video-on-demand trial offer to viewers in Queens, N.Y. from Nynex and Time Warner's cable division features soft-core porn movies.

The pay-per-view skin flicks, available since mid-November, are part of the Spice Channel, an



SLEAZE, PLEASE: *Don't XXX in Queens*

mult-program service that is part of the Time Warner package offered to 22 households participating in the trial offer. Under federal regu-

lations, phone companies have no say over the content of video services carried over their lines.

Time Warner says viewers can keep their kids from calling up Spice offerings by not telling them the special identification number needed to order a movie. Nynex, which is only acting as the delivery method for the Time Warner service, has expressed no pub-

lic chagrin over it. But Nynex says it is seeking a way for subscribers to block the channel altogether if they wish. *Catherine Arnst*

DRAWN & QUARTERED

WISSTMAN
DRAFT
FIND YOUR



MOM!
A NEW
ATE KERMIT
THE FROG!

CASINO CULTURE

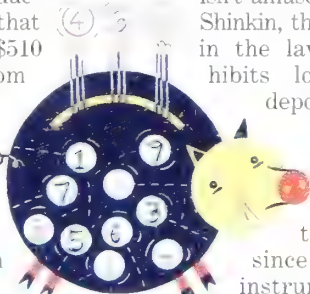
A LOTTO NERVE AT JAPANESE BANKS

WIN THE LOTTERY AT A BANK? You can in Japan. Johnan Shinkin Bank, a scrappy Tokyo credit cooperative, has defied staid Japanese bank regulators by introducing time-deposits that pay prizes up to \$510 based on random drawings. Depositors have flocked to Johnan, bringing in \$1 billion since the lottery-deposits were offered on Nov. 7.

The gimmick has Johnan Shinkin's competitors fuming. Takashi Tamaki, head of the Regional Banks Assn., complains that banks should be helping customers "by im-

proving services and raising interest rates, not with prizes." His group and another small-bank federation had warned members not to follow Johnan Shinkin's example, but Japan's Fair Trade Commission told the groups to back off. Although the powerful Finance Ministry isn't amused by Johnan Shinkin, there's nothing in the law that prohibits lottery-linked deposits.

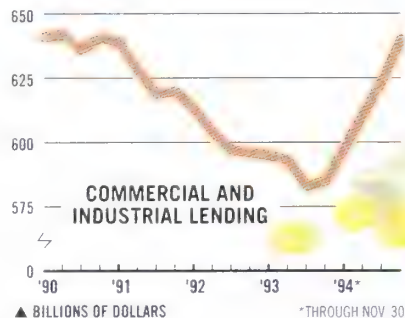
Meanwhile, 49 other small lending institutions have since cooked up instruments using the lottery gimmick. And the Federation of Bankers Associations, which represents Japan's large banks, just lifted its ban on cash prizes. *Larry Holyoke*



THE BIG PICTURE

BACK IN THE MONEY

Even when the recession ended in March, '92, commercial banks were tight with business borrowers. But strong corporate earnings have persuaded banks to loosen up their lending.



▲ BILLIONS OF DOLLARS

*THROUGH NOV 30

DATA: FEDERAL RESERVE

NOTES Retirees, in survey, who like retirement better than expected: **70%**. Retirees who would rather be working: **45%**

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wait. That's one more bubble that's almost certain to burst.

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Lufthansa could have called on any bank to help them further privatize in October, 1994. But then, Lufthansa doesn't like turbulence. So they called their preferred "Tower" to arrange and lead the deal: Dresdner Bank.

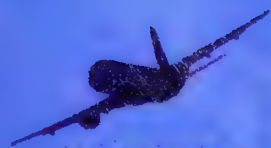
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A GIANT STEP INTO CYBERSPACE

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Jan. 9, 1995

TABLE OF CONTENTS



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TALK



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WHAT'S NEW

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READY, SET...CLICK:
Last week, BUSINESS WEEK was launched on America Online

BUSINESS WEEK's worldwide audience of nearly 7 million has just broadened dramatically: The magazine is now available electronically to the 1.5 million members of America Online, the fastest-growing computer online service.

Last week's issue, featuring the 1995 Industry Outlook, was the first to go up on AOL screens, and the contents of all editions will now be available every Thursday night, ahead of the earliest newsstand and subscriber deliveries.

The new service, called BUSINESS WEEK Online, includes not only the full text of all articles, along with selected illustrations, but also many extra features such as interactive message boards, a chat room, and weekly online conferences with editors and newsmakers. In Who's Who Online are short biographies—and in most cases pictures—of many of the editors who will be active online. You can also learn all about 44 business schools (an expansion of the popular biennial Best B-Schools rankings), browse—and buy—business books, and much more.

The partnership with AOL is

BUSINESS WEEK's biggest step so far into cyberspace. But its articles have long been available on databases such as Dialog and Nexis. And since last May, each week's table of contents and at least one story have been posted on the Internet on the Electronic Newsstand.

It's typical of the magazine's spirit that the AOL project was the effort of an enthusiastic team, led by Vice-President for Strategic Planning & Development Cara Erickson as general manager and by Senior Editor Bob Arnold as editor of BW Online. John A. Dierdorff, who retired in 1993 as managing editor, is consulting editor. Art Director Malcolm Frouman and Graphics Director Arthur Eves played major roles. The technical intricacies were mastered by John E. Johnsrud, McGraw-Hill vice-president for systems planning and technology.

For a free trial disk from AOL, call (800) 641-4848 and mention BW Online. We hope to see you often online as well as in these pages.

Stephen B. Shepard

Editor-in-Chief

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SENATOR BUMPERS: WE'RE ARMED TO THE TEETH

"The Pentagon's real readiness crisis" (News: Analysis & Commentary, Dec. 19) is wrong to assert that spending cuts mean that U.S. troops may have to go into some future conflict stuck with yesterday's weapons."

Even though the Soviet threat is one, our forces are much better quipped today than at the end of the old war. They will continue to improve—with more than \$100 billion worth of new weapons in the pipeline, including three supercarriers, three ballistic-missile submarines, eight nuclear attack subs, a squadron of B-2 bombers, plus scores of F-15, F-16, and F-18 fighters. All are superior to their counterparts elsewhere in the world.

During the rest of the 1990s, we will spend as much on military research and development as during the late 1970s, when we designed the generation of weapons that performed so successfully in Operation Desert Storm. The Pentagon will spend more than \$1.5 trillion during the next five years. As long as we don't waste money on hugely expensive weapons no longer needed, this will be more than enough to maintain our readiness and overwhelming technological superiority.

If this isn't enough, it'll be because we presided over the greatest mismanagement of defense spending ever. Is it not incredible that we spend as much on defense as the rest of the world combined, and yet people like you suggest we're becoming a "hollow" military?

Dale Bumpers (D-Ark.)
U. S. Senate
Washington

PUTTING KUTTNER TO THE QUICK IN CAPITAL GAINS

I believe small-business owners would disagree with Robert Kuttner's premise that a capital-gains tax cut would be a gift to the rich, not the middle class "Capital gains: Here's one the Democrats can win," Economic Viewpoint, Dec. 19).

The rich, whenever possible, avoid such taxes by taking their losses and setting their gains run. The small entrepreneur, however, usually has his equity tied up in one undertaking. If he sells out, he is immediately up to 28%

poorer both in earning power and net worth because of capital-gains tax.

This restriction on the mobility of capital limits small-business owners' ability to build net worth and move up to other opportunities. These members of the middle class—the backbone of our free-enterprise system—labor mightily over the years, plowing after-income-tax dollars back into their businesses in order to grow. Isn't one tax on capital formation enough? The U.S. is one of the few countries in the world to tax capital growth twice.

Jerry Huse
Publisher
Norfolk Daily News
Norfolk, Neb.

Kuttner says: "With such a generous tax cut, no conceivable increase in stock sales would make up the revenue loss."

But according to figures from the Congressional Budget Office, tax cuts in the early 1980s produced gains in revenue (chart). This shows Kuttner's statement is based on his own version of the facts and not on history.

Gregory J. Emmerth
Atlanta

Kuttner's article is interesting, but like many treatises, it misses the essence of who pays capital-gains tax.

The piece assumes that such taxes are paid by the wealthy. In reality, however, most capital gains are earned on financial instruments owned by the middle class: mutual funds, retirement annuities, and other vehicles.

In the 1992 race, George Bush failed to respond to the Democrats' claim that capital-gains cuts would benefit the rich. He should have known better. The real issue is "Capital gains: Here's one the Republicans shouldn't lose."

Michael A. Mogavero
Dean
School of Business
Dowling College
Oakdale, N. Y.

Whatever objections there might otherwise be, a tax cut makes good sense if applied only to long-term investors. As a recent Twentieth Century Fund report suggested, a capital-gains tax that is steeply graduated—falling dramatically as the holding period lengthens—would discourage the short-term outlook that's the bane of financial markets. This long-discussed proposal would

also mitigate the revenue loss otherwise entailed.

Louis Lowenstein
Professor of Finance & Law
Columbia University School of Law
New York

THE SLIPPERY SEMANTICS OF "SKIER-DAY"

Congratulations on recognizing that the term "skier-day" could use clarification ("Can't we all just schuss together?" Up Front, Dec. 19). Unfortunately, the explanation ("that's one skier per day") confuses "per" with "for one."

"Per" divides one unit by another, as in "words per page." But "for" multiplies units, as in "two skiers for a three-day stay"—which yields six skier-days. The correct meaning of a skier-day is "one skier for one day."

Edward MacNeal
Wayne, Pa.

BAUSCH & LOMB THROUGH A WIDE-ANGLE LENS

Mark Maremont did an excellent job capturing the essence of marketing and sales programs in "Numbers game at Bausch & Lomb" (The Corporation, Dec. 19). But many of his conclusions and innuendos are way off base. As a Bausch & Lomb contact-lens and Ray-Ban distributor, I tell you the worst they're guilty of is a marketing program that didn't materialize. You've made one small episode in a fine company's history seem like the whole place is rotten.

Herbert S. Natkin
President
New Era Optical Co.
Chicago

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TROUBLED TIGER

Businessmen, Bureaucrats, and Generals in South Korea

by Mark L. Clifford

J.E. Sharpe • 357pp • \$55/ \$19.95 paper

CAN KOREA PULL THE THORN FROM ITS FOOT?

As the developing world searches for a new economic model after the collapse of socialism, technocrats from Beijing to Cairo gaze enviously at South Korea. Thanks to meticulous planning, Korea transformed itself in three decades from one of the world's poorest nations to one poised to join the ranks of the richest. It is the only Third World nation to become

a global export powerhouse with its own brands of semiconductors, appliances, and cars.

But can the state-led, highly nationalist policies of the late dictator Park Chung Hee work for other countries in the increasingly integrated global economy? For that matter, can they keep working for Korea? Not in the view of Mark L. Clifford, business editor of Hong Kong's *Far Eastern Economic Review*.

In *Troubled Tiger: Businessmen, Bureaucrats, and Generals in South Korea*, Clifford credits much of Korea's success to a level of protectionism and state control that trading partners and international leaders probably wouldn't tolerate if they were launched today.

Indeed, despite its wealth, South Korea seems incapable of soon embracing the global movement toward a free flow of goods, technology, and capital, says Clifford. And while Japan still seems able to get away with such mercantilism, South Korea lacks Japan's manufacturing prowess and huge capital surpluses. Unless Seoul remakes its system, says Clifford, its mighty *chaebol*, or business groups, "will be pushed to the sidelines of the international economy."

Although such gloom seems excessive, given South Korea's 7% annual

rate of economic growth, *Troubled Tiger* is one of the better books on the Korean "miracle." Clifford has made his political-economic history surprisingly gripping by focusing on the fascinating people behind the policies—among them strongman Park, who ruled with both brutality and inspiration for two decades, and the impressive cast of technocrats who took over after his 1979 assassination.

A former Seoul correspondent, Clifford interviewed key technocrats to develop the big picture. His narrative is made compelling by the many calamitous events that rocked Korea in the 1980s and influenced its economic path—the military's 1980 massacre of protesters in Kwangju, the destruction of Korean Air Flight 007 by the Soviets, the 1983 Rangoon bombing that killed 17 Korean

officials, and a raft of scandals that followed the end of military rule in 1987.

The book is refreshingly balanced. The reader gains great respect for the boldness and vision of Park, who put Korea on the map with high-risk bets on huge steel mills, shipyards, and auto complexes. Even as state-led efforts to develop advanced industries in India, China, Eastern Europe, and Brazil failed, Korea's succeeded, largely because Park made companies focus on exports. Products had to meet international standards of quality and cost-efficiency, and companies that failed in world markets had their credit cut off.

The reader even develops sympathy for the much maligned Chun Doo Hwan, who ruled for seven years after seizing power in 1980. A military man who knew his limitations, Chun submitted

diligently to extensive late-night tutoring by economic planners.

But Clifford also lays out the brutal side of Korea's triumph—the oppression of dissidents and unions and the coercion of the private sector. While Japan's business groups have their own banks, Korea's financial system was state-monopolized, so government planners dictated every facet of industry and trade. To keep access to credit, companies had to make huge "donations" to the ruling party and, under Chun, to "charities" fronting for his family.

Where Clifford falls short is in backing up his assertion that Korea is unlikely to change. He is hardly alone in seeing Korea's economy as burdened by structural weaknesses. And countries that might follow Korea's example are wary of interventionist policies, though such moves can jump-start development.

But Clifford devotes few pages to analyzing Korea after democracy. He is dismissive of Kim Young Sam, who became President in February, 1993. Kim has been timid about honoring promises to cut state interference in the market. And because he has used trials, ostensibly politically motivated, to persecute executives tied to Park and Chun—such as Hyundai Group founder Chung Ju Yung—Clifford views him as just one more mandarin suspicious of businessmen. Most leaders, Clifford writes, have "at best, a lukewarm commitment to a new way of doing business."

This assessment seems hasty. Since early 1994, when Clifford ended his research, there have been many signs that Korea is proceeding with plans to bring its foreign-investment laws, trade codes, and capital markets in line with international standards of openness by 1998. And, as Clifford shows, Korean planners over the past 20 years have been willing to take tough action to preserve economic health.

And the economy? In 1994, it grew 7.8%, and it should grow by at least 7% again in 1995. Korea's auto and semiconductor industries continue to overcome periodic setbacks and increase global market share. Still, readjustment under democracy won't be easy. *Troubled Tiger* excels at showing the high price of a long obsession with growth.

BY PETE ENGARDIO

Hong Kong Correspondent Engardio reported from South Korea in the early 1980s.

CLIFFORD ARGUES THAT SEOUL MUST RELAX ITS CONTROL OVER INDUSTRY TO KEEP ROARING

EDITED BY STEPHEN H. WILDSTROM

PAGERS THAT CAN SPELL IT ALL OUT

A few years ago, anyone you saw wearing a beeper was apt to be either a doctor or a technician on call. These days, beepers—or, to give them their proper name, pagers—adorn the belts and pocket-books of all sorts of people. For many executives and professionals on the go, pagers—which usually vibrate rather than beep—have become invaluable companions. And new pagers and paging services now coming along will greatly enhance their usefulness.

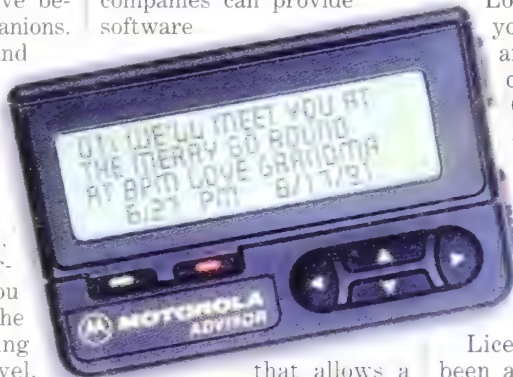
Pagers have grown up. The earliest units did nothing but beep, usually at an embarrassing moment. You had to phone to get the number of the calling party. The next level, pagers that provide the number to call, still account for at least 80% of the units in use.

HEADLINES. Alphanumeric pagers, which can spell out a message, account for only about 12% of new sales but dominate the executive market. The top-of-the-line Advisor from Motorola Inc. lets you scroll through text messages four lines at a time, allowing for expanded communications. And because pagers are priced like cellular phones, with service providers heavily subsidizing the purchase price, even the fanciest unit should set you back less than \$100 when you buy it with a service agreement.

For many, perhaps the most important use of pagers comes in partnership with a cellular phone. Fishing a

ringing phone out of your briefcase or purse is awkward at best, and leaving the unit on standby to receive incoming calls gobbles up batteries. Give callers your pager number instead, and use the cell phone only to call out.

The use of pagers, however, goes well beyond taking phone messages. Paging companies can provide software



that allows a modem-equipped computer to send a text message to your pager. You can also arrange to get selected news items from Reuters or from other news services (prices and availability vary). For example, I could have a pager receive certain headlines, say, those referring

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You can also have electronic mail sent to a pager. Both cc:Mail and Lotus Notes, for example, can be set up to page you when a high-priority E-mail message arrives. You can then whip out your laptop to retrieve the text or, with some Notes systems, receive the messages themselves by phone.

"CANNED" REPLIES. Paging is offered in a baffling array of service plans and prices. The basic rates allow you to receive a set number of messages per month on a pager you buy or rent, with an additional charge for each extra message. Your most important decision is coverage:

Local service will page you only in your home area; national paging, offered by MobileComm, SkyTel, and PageNet, will reach you anywhere in the U.S. Some services provide a third option that requires you to notify the paging company where you'll be.

Licenses that have just been auctioned by the federal government will provide new paging options, perhaps by the end of 1996. The new "narrowband PCS [personal communications services]" pagers will have a limited two-way communications ability. One benefit is that these new pagers, like cellular phones, will be able to tell the network where they are, making national paging more efficient. You'll also be able to acknowledge receipt of pages and to select from a menu of "canned" responses to messages.

Pagers may not be the highest-tech communications devices around. But unlike wireless technologies such as cellular data transmission, they are affordable and here today. If you need to stay in touch, a pager may be just the right tool for you. S.W.

BULLETIN BOARD

SOFTWARE

TIME MARCHES OFF

The millennium will likely give a lot of people pause—but especially those who run some old software on their computers. They'll have to prepare for the future in their own way because their programs won't be able to cope with a year starting with 20.

Back when storage space



was tight, a lot of programmers tried to save a few bytes by assuming the first two digits of a year were always 19. Reader Joseph Warren, a Burlingame (Calif.) computer consultant, warns that the problem is worst in main-frame programs written in the COBOL language, especially accounting or payroll routines. Current off-the-shelf software should handle the new millennium fine, but custom applications written for database managers, such as Borland's dBase, could have problems.

PASTIMES

SKETCHING CYBERSCAPES

Looking for a way to unwind at your PC but want a pastime more dignified than Solitaire? If you're a Macintosh user, you might consider KPT Bryce from HSC Software (805 566-6200). The \$150 program uses sophisticated mathematical techniques that allow complete novices to draw realistic or surrealistic landscapes. The program is simple to use, and it's positively hypnotic to watch the computer render your scene.

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BY RUDI DORNBUSCH

WE HAVE SALINAS TO THANK FOR THE PESO DEBACLE



MIRAGE: Salinas and crew upheld the myth of a Mexican supereconomy. But all along, a pumped-up peso was strangling growth

The crash of the Mexican peso is just one more example of the cycle of delirious optimism followed by collapse and bottomless gloom in Latin American finance. The peso's fate has ruined investors' end-of-year bonuses and is a major setback to Mexico's prospects. A postmortem is instructive. The blame lies squarely with former President Carlos Salinas de Gortari.

Mexico last crashed in 1982, following a borrowing spree in the late 1970s. Debts to commercial banks around the world went into default; the peso was devalued again and again in an attempt to gain a trade surplus to meet the demands of creditors. But even as the currency went down, inflation exploded. That vicious cycle of inflation and depreciation peaked in 1987 with inflation well above 150%. Pressured by events, reform and stabilization became the central objective. Much good was done: privatization, trade liberalization including the North American Free Trade Agreement, deregulation, and budget balancing including fiscal reform.

FOOL'S GOLD. External confidence recovered, investment money started to return, external deficits ballooned. With easy access to financing and much of the domestic agenda accomplished, reducing inflation to U.S. levels became the central preoccupation. Depreciation of the peso was unwisely kept far below the rate of inflation, a policy that helped slow inflation but also meant an increasingly uncompetitive trade position. At the outset, that could be rationalized by renewed access to world capital markets and the rewards of a reformed and stabilizing economy. But at some point, competitiveness had to be restored. By 1993, Mexican producer prices expressed in dollars had risen by more than 45% compared with prices in the U.S. Clearly the peso had become overvalued, but Mexican leaders refused to acknowledge the facts, and foreign investors were lulled into holding on to exposed positions.

Salinas and his policy team reasoned that real appreciation held no problems: NAFTA would bring direct investment and trade opportunities. Deficits were large now but would be small in the future. In any event, money was not thought to be a problem because international investors had developed a mad crush on Mexican stocks and treasury bills. Overvaluation became troublesome when the upcoming 1994 election brought

with it the possibility of changes in economic strategy or a show of weakness by the official party. Indeed, politics turned nasty (the Chiapas uprising and two assassinations), causing some eyebrows to raise. But investors were assured daily that all was well: The peso would never be allowed to fall. The foreign loans kept coming, but at higher interest rates, which combined with lack of competitiveness to strangle growth. No growth plus a gigantic external deficit—some 6% of gross domestic product—made it certain the peso would yield sooner or later.

QUICK FEET. Yet Salinas persevered with his strategy of politics first, reality later, and the peso remained disastrously overvalued. The myth of a superperforming Mexican economy was kept alive. Criticism was not brooked, especially by Cabinet ministers who nursed an ambition to be the next holder of absolute power. Chilean dictator General Augusto Pinochet painted himself into a similar corner in the late 1970s. Just as Pinochet and his toadies ignored common sense in currency matters, Salinas believed that with enough manipulation and censorship he could keep the peso afloat. In the end, both turned out to be wrong in a strikingly similar manner.

Without Chiapas, the crisis might never have happened. But there is always some extraneous event that makes the glass run over. If the currency is badly out of line, it doesn't take much. But why the seemingly bottomless drop of the peso that is occurring now? Here, the analogous situation is a bank run. Mexico dissipated its reserves in an attempt to sustain various unrealistic levels of the peso. In such a predicament, no one wants to be the last one out—or the first back in: Investors fled en masse. Ultimately, they will return, but only when assets are dirt cheap. Just as in real estate, there is always another boom: It just doesn't come in time to help the holders of the hot potato.

Mexico's per-capita income today is still 5% less than it was in 1982, at the time of the last crisis. The easy money is gone, and real income will be falling further. The brilliant reforms implemented by Salinas were about to put his nation on the path of prosperity; his utterly misguided currency experiments instead plunged the country into economic and possibly political turmoil. Mexico will enter the next century far poorer than it was two decades ago.

Rudi Dornbusch is professor of economics and management at Massachusetts Institute of Technology.

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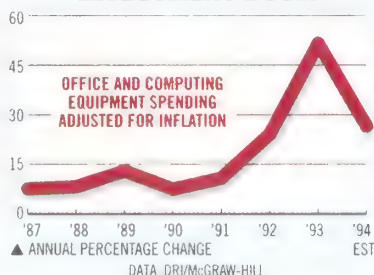
IS THE COMPUTER BOOST THAT BIG?

They may not spur output greatly

Why has U.S. productivity been resurgent in the 1990s? Better management? Slimmed-down bureaucracies? Fewer workers? To a growing number of economists, the most important reason is the spread of computers and other high-tech equipment in the workplace.

But Daniel E. Sichel, an economist at the Brookings Institution, and Stephen D. Oliner, an economist at the Federal Reserve, think the impact of computers on recent productivity growth has been vastly overstated. In a

AMERICA'S BUSINESS INVESTMENT BOOM



forthcoming *Brookings Papers on Economic Activity*, Sichel and Oliner calculate that from 1987 to 1993, computers and peripheral equipment contributed at most only 0.2 percentage points a year to growth in business output, after adjusting for inflation. That's not much considering real business output expanded by 1.9% a year between 1987 and 1993. Adding in software and labor does boost the contribution of computer services on productivity to a more significant 0.4% a year—a figure that could rise to 0.5% annually from 1993 to 2003.

The reason computers contribute so little to higher productivity and output is surprisingly simple: Despite the digital explosion of the past 15 years, the installed base of computers still constitutes a tiny 2% share of the nation's total capital stock, according to Sichel and Oliner.

The economists also note that the contribution of computers to net output may have been far less than is typically calculated. When companies take heavy depreciation charges as old computers are scrapped every few years in favor of newer, faster models, it sharply reduces

the economic growth attributable to high-tech gear. "I'm not suggesting computers haven't brought about efficiency gains for individual corporations," says Sichel. "It's just not the story for the economy as a whole."

IMPORTS AND GDP: A RECOUNT

Federal data may be skewed

Trade experts have been troubled by the tendency of Americans to spend discretionary-income gains on imported goods—like Japanese cars and Korean VCRs. Indeed, the conventional economic calculation is that every percentage-point rise in America's gross domestic product generates a 2.5% surge in import demand. This link is why economists fret that much of the windfall consumers may realize from congressional tax cuts in 1995 will end up in the pockets of overseas producers.

Maybe not. The presumed correlation between changes in GDP and imports may be overstated, according to a National Bureau of Economic Research paper by University of California at Davis economist Robert C. Feenstra and International Monetary Fund economist Clinton R. Shiells. They suggest that a percentage-point hike in GDP lifts demand for foreign goods by a more modest 1.7%.

The authors say the government is relying on a flawed methodology for compiling its import data. In particular, import price indexes constructed by the official statisticians don't adequately take into account changes in what Americans buy from foreign suppliers. The government doesn't include new varieties of products offered at lower prices. (This argument parallels most economists' belief that the consumer price index overstates the annual inflation rate by at least 0.5 percentage points.) The result: America's terms of trade with other nations may have been better than reported and the benefits of trade underestimated.

A CREDIT-CARD CONUNDRUM

Why rate cuts add to lender risk

Historically, credit-card issuers have been notoriously slow to slash the interest rates they charge consumers. Each week, it seems, a mailing arrives

from an aggressive entrant in the credit-card business offering a rock-bottom "teaser" rate. Other competitors offer rebates on such items as cars or plane tickets. Still, it's relatively rare for credit-card companies anxious to build market share to simply lower their rates—as hungry players in other industries do.

It may well be that the economics of price-cutting backfire in the credit-card business. Companies chasing new customers with low rates simply lose profits, according to Loretta J. Mester and Paul S. Calem, economists at the Federal Reserve Bank of Philadelphia. Using the Federal Reserve's rich database on consumer finances, Mester and Calem show that the customers most likely to shift because of a rate cut are the riskier ones. They're looking to escape their crushing debt load built up on the high interest rates charged on their current accounts.

By contrast, a card issuer's most profitable customers—people with high balances and good credit ratings—are unlikely to change issuers because of low rates. These desirable customers are loath to lose the high credit limits they've built up with their current issuer.

PLENTY OF BANG FOR THE BUCK

The dollar's mighty buying power

In this era of diminishing expectations, the latest World Bank survey of incomes in 209 nations offers some encouraging news. Yes, American workers are in seventh place in the world measured by per capita income (\$24,750 vs. \$36,410 in world-leader Switzerland). But measured by living standards, using purchasing-power parity calculations to smooth out the effects of currency swings and different price levels, the U.S. ranks second only to Luxembourg in what its incomes will buy, \$24,750 vs. \$29,510, and way ahead of Japan and Germany. On a more distressing note, 14 of the 15 republics of the former Soviet Union lost ground in 1993.

A STRONG SECOND FOR THE U.S.

1993 PER CAPITA INCOME ADJUSTED FOR PURCHASING-POWER PARITY, IN DOLLARS

LUXEMBOURG	\$29,510
U.S.	\$24,750
SWITZERLAND	\$23,620
UNITED ARAB EMIRATES	\$23,230
QATAR	\$22,910
HONG KONG	\$21,670
JAPAN	\$21,090
GERMANY	\$20,980
SINGAPORE	\$20,470
CANADA	\$20,410

DATA WORLD BANK

BY JAMES C. COOPER & KATHLEEN MADIGAN

WHY SOME BUSINESSES MAY FEEL CHEATED THIS YEAR

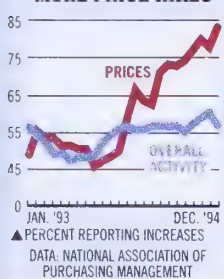
U.S. ECONOMY

Corporate America in 1995 could end up feeling like the Penn State football team. Companies are doing everything right, but they still might miss out on the big prize.

Businesses have worked hard to cut costs and boost productivity, which has enhanced their competitiveness abroad and bolstered their profitability. But just like the Nittany Lions, who went undefeated but lost the national championship to the Nebraska Cornhuskers, companies this year may find that their efforts to improve sales and profits will go unrewarded.

The spoiler is shaping up to be the Federal Reserve. To keep inflation down, the Fed will continue to raise interest rates in order to slow the economy. Higher borrowing costs will hit the goods-producing side of the economy—notably manufacturers and builders—especially hard. That's not tough to figure: Durable goods, from turbines to cars to furniture as well as construction projects, are usually bought on credit.

PURCHASERS REPORT MORE PRICE HIKES



GDP down to the Fed's target of sustainable but noninflationary growth.

Last year's shift in monetary policy will also take some cash out of the pockets of consumers and corporations. Consumers can expect to see rising finance charges on everything from mortgages to auto leases to credit-card bills. And adjustable-rate mortgages will be refigured higher, sapping more money out of the monthly budget.

THE FED-ENGINEERED

slowdown will hold back revenues and earnings. Corporate America enjoyed a banner year for profits in 1994, but that is unlikely to be repeated in 1995. Indeed, the 1995 economy is shaping up to be a bleached copy of 1994: less growth, smaller job gains, and slightly higher inflation.

Industrial activity already showed some fatigue in December, according to the National Association of Pur-

chasing Management, even though prices of industrial materials continued to rise (chart). The NAPM's index fell to 57.8% last month from 61.2% in November. While the overall index is still high, the purchasers reported declines in their production and employment indexes at yearend.

The overall new-orders index also fell in December, but export bookings rose. That suggests that the slowdown in demand is concentrated at home. Most likely, the buildup in inventories at retailers during the holiday season has caused stores to hold off on reordering. The strength in export orders means that manufacturing will slow, but not sink, in coming months.

FOR INFLATION WATCHERS

at the central bank and in the financial markets, the most alarming facet of the NAPM report was the unrelenting rise in prices. The NAPM price index jumped from 77.9% in November to 83% in December—the highest reading in almost 15 years.

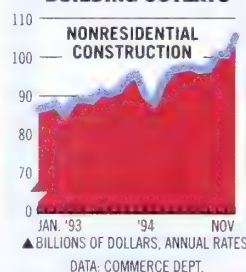
Also disturbing was the rise in the supplier-deliveries index, to 64.9% from 64.4%. That means businesses are waiting longer for their suppliers to ship out orders. In fact, delivery performance is at its poorest in six years. That suggests production bottlenecks are forming, which could enable manufacturers to lift prices.

But whether these price hikes stick—and whether they can be pushed forward in the supply chain—will depend on demand. By all indications, the Fed will continue to raise interest rates to slow domestic spending. Home builders are already feeling the pinch, though construction has held up surprisingly well given the rate hikes of 1994.

Warm weather helped lift construction in November. Spending on building projects increased 0.7%, the fourth consecutive gain. But even though home building rose only 0.5% in the month, outlays for business construction jumped 4.8%, as a pickup in nonresidential spending continues to buoy the building sector (chart).

That's also the indication of the latest data on construction contracts. The F.W. Dodge Div. of McGraw-Hill Inc. reports that contracts for nonresidential buildings were up 10.9% in November; with retail projects up 19%. Contracts for residential building dropped for the third consecutive month in November. They fell 2.2% in Novem-

BUSINESSES LIFT BUILDING OUTLAYS



ber and are down 14.6% from their peak of November, 1993. Total contracts rose 2.8% in November.

The drop in residential contracts reflects weaker housing demand. Sales of new single-family homes fell 2.5% in November, to an annual rate of 693,000. The temperate weather lifted sales in the Northeast and Midwest, but buying plunged 16.1% in the much larger Western market. Also, the supply of built but unsold homes expanded in November.

Industrial and office projects will take up some of the slack caused by housing. The ongoing boom in capital spending and the increase in industrial operating rates are lifting business construction. Also, the economic expansion helped soak up the large amounts of vacant office and retail space that cluttered the commercial real estate picture in the early 1990s.

For 1995, nonresidential construction should continue to do well. Of course, weather plays a greater role in construction than in any other part of the economy, and higher interest rates may table some commercial projects. But the need to expand factories, build retail space, and upgrade office facilities should keep the building sector afloat.

OTHER BUSINESSES SHARE an upbeat view of 1995. Corporate executives are feeling extremely confident about the prospects for this year, reports the U.S. Cham-

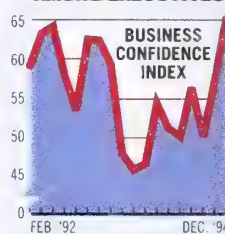
ber of Commerce. Its index of business confidence bounced up to 65.2% in December from 57.2% in October (chart). The bimonthly index is just 4½ years old, but the current reading is the highest in this expansion.

What's lifting the spirits in the corner office? The Republican victory for one thing. The Chamber reports that 79.5% of the respondents felt that recent election results will improve the business climate. In addition, more than half expect increased sales in the first half of 1995, and 46.3% figured that the economy would keep growing.

Even projected job growth showed a bit of strength: The percentage expecting some new hiring rose to 27.6% in December from 24.2% in October. However, the vast majority of businesses—65.2%—foresaw no change in their payrolls over the next six months.

In fact, businesses will still keep a keen eye on their labor costs this year. That's what helped them to such a profitable year in 1994. This year, companies are sure to stick with their winning strategy. But trying to gain ground against the Fed's stingy defense will be a whole new ball game.

OPTIMISM GROWS AMONG EXECUTIVES



DATA: U.S. CHAMBER OF COMMERCE

EUROPE

BRITANNIA RULES A WAVE OF GROWTH

Britain's economy rolls into 1995 on the crest of its best performance in decades. Growth, at better than 4%, is the strongest in six years, unemployment is down from a peak of 10.6% two years ago to 8.8%, and both the fiscal and current-account deficits are improving, while retail inflation is a low 2.2%.

Can these happy days continue in 1995? It looks that way. Despite a likely subdued showing by consumers, reflecting a second year of higher taxes for the year ending in April, exports and capital spending are set to lead growth. A stronger-than-expected world recovery and gains in competitiveness from sterling's decline

two years ago will buoy foreign shipments. Solid demand, rising utilization rates, and fatter profits will lift plant-and-equipment outlays. Many analysts are betting that growth will outpace the 3.2% consensus expectation.

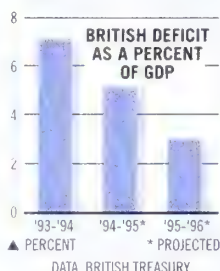
Of course, inflation has always played the spoiler in Britain's economy—but this time looks different. The Organization for Economic Cooperation & Development has estimated that there is enough spare output capacity to allow growth at the current 4% pace for two more years before hitting inflationary limits.

Moreover, government policy is anti-inflationary. The Nov. 29 budget for fiscal 1995-96 retained both

the previously announced tax hikes and the trend of spending restraint, while offering a plan to cut long-term structural unemployment. Although Parliament's Dec. 6 rejection of a planned increase in home-fuel taxes lopped off about 25% of this year's tightening, the Treasury offered offsetting hikes. The government expects the deficit to shrink to 3% of gross domestic product in 1995-96 (chart).

Out of concern that strong growth will fuel inflation, the monetary authorities have already raised interest rates twice, and more hikes seem likely in the first half. Even if the government cuts taxes prior to a likely 1996 general election, it's a good bet that tighter monetary policy will take up the slack, helping to maintain growth with low inflation.

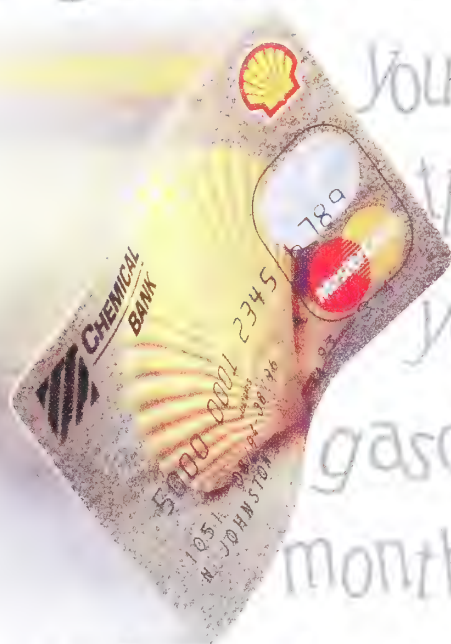
FISCAL TIGHTENING REMAINS IN PLACE



▲ PERCENT DATA: BRITISH TREASURY * PROJECTED

ZERO TO FREE GASOLINE IN NOTHING FLAT.

The Shell MasterCard[®] from Chemical Bank lets you start earning free FormulaShell gasoline as soon as



You start using the card. And you get that gasoline next month. Not next

year. And that's just the beginning. It takes nothing more than a quick call to apply. So, what are you waiting for? **1-800-FREE-GAS.**

earn unlimited Shell gasoline using the Shell MasterCard. Rebates automatically applied to monthly statement. For details, drop by a Shell service station for an application. See Rebate Terms and Conditions. Void where prohibited by law. Gasoline rebates not redeemable in New Jersey. The APR is 17.8%. There is a \$20 annual fee, and a minimum 50¢ finance charge for purchases if a finance charge is imposed. There is a 2% cash advance fee, not less than \$1 nor more than \$10. This information is accurate as of December 1994, the date of printing, and is subject to change without notice.

CONGRESS

LET THE WILD RUMPUS START!

As the GOP takes power, small and big business jostle for position

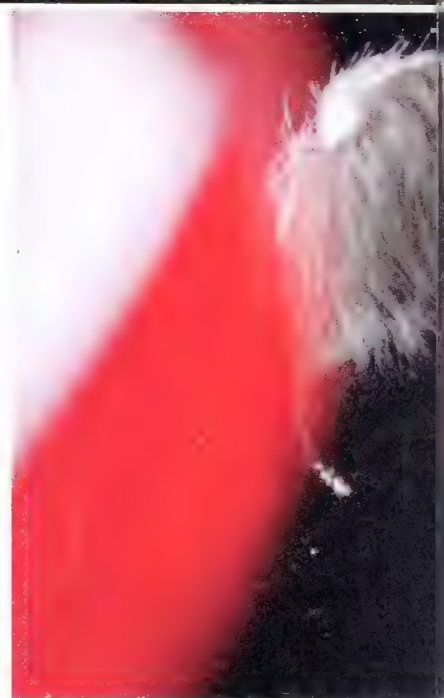
On Jan. 4, when Speaker Newt Gingrich gavelled the first Republican-controlled House of Representatives in 40 years to order, he ushered in a new era for American business. After decades on the defensive, corporate chieftains and Main Street entrepreneurs alike felt liberated from the political imperative of kowtowing to Capitol Hill Democrats.

Executives of companies big and small are chanting the same mantra: Slash spending, cut taxes, eviscerate government regulation. But while they applaud Congress' new direction, business groups differ over how far to push change. While major corporations want to tinker with a status quo they've learned to master, small business owners want to rewrite the rule book. As a result, lobbyists for the two camps are girding for some nasty trench battles. "When it gets down to the nitty-gritty of writing bills, we're going to see some pushing and shoving," predicts Jack Faris, president of the National Federation of Independent Business.

That's because the House is firmly in the grip of populists led by Gingrich and Majority Leader Richard K. Armey (R-Tex.), both small-business champions who have clashed with Establishment executives. Big business is counting on Senate Majority Leader Bob Dole (R-Kan.) to rein in revolutionary excesses. The Senate "will be providing the brakes for some of the radical proposals from the House Republicans,"

Senate Minority Leader Thomas (D-S.D.).

One early test will be the jockeying over tax cuts. Big and small business alike crave capital-gains tax cuts but differ on other items. Small business lines up behind the House Republicans' Contract With America, including provisions to deduct up to \$25,000 for equipment and inventory, increase the estate-tax exemption for small business, and repeal small-business tax hikes contained in the 1993 Clinton economic plan. Big Business prefers accelerated depreciation, along with targeted research-and-development credits. And in the end, much of Corporate America is more concerned about reducing the deficit than getting new tax goodies. "The deficit is getting sufficiently out of control, and that's causing a negative business climate," warns Robert C. Kirkwood, a lobbyist for Hewlett-Packard Co.



GOP lawmakers mean to slash the deficit, but Big Business may not be happy with every target. Favorites on the chopping block: farm subsidies and export-marketing programs. Farm-subsidy foes, led by Armey, assail the program as socialism that reeks of "Moscow on the Potomac." Agribusiness, meanwhile, is counting on longtime friends, including Dole and House Agriculture Committee Chairman Pat Roberts (R-Kan.), for protection from an assault by budget-cutting conservatives and urban liberals. "The U. S. is a

The New Congress

When it comes to hashing c

BIG BUSINESS



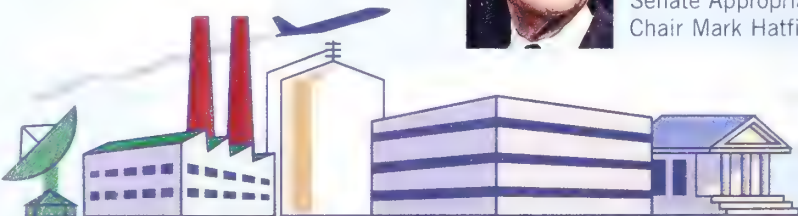
FARM SUBSIDIES Agribusiness counts on Senate Majority Leader Bob Dole, longtime champion of farm interests, to repel GOP attacks on program.



AFFIRMATIVE ACTION Call live with antidiscrimination guidelines that may be taken up by Judiciary Chair Orrin Hatch because they would protect corporations from bias suits.



EXPORT PROMOTION Hop to preserve Commerce Dept. subsidies to market U.S. products abroad. A key backer Senate Appropriations Chair Mark Hatfield.



Gingrich has always been a friend to small business, and that may make Corporate America edgy

lear world leader in agriculture, and it is important that we not damage the industry," says Robert E. Fowler, chief executive of Vigoro Corp., a Chicago-based fertilizer maker.

At the same time, multinationals hope to protect Commerce Dept. grants that promote U.S. products abroad. Backers say the grants level the global playing field, but entrepreneurs insist that Big Business pay its own tab. "There is no reason to give tax money to Sunkist and McDonald's or promote their products," says Kar-

en Kerrigan, president of Small Business Survival Committee.

On regulatory reform, small businesses favor radical changes in the GOP Contract. They back efforts to limit overall compliance costs to 5% of gross domestic product by slashing environmental, workplace safety, and other federal rules. Philip Bourgeois, president of Studio Red, a 20-person design firm in Redwood City, Calif., says enough is enough: "If I was any more regulated, I don't know if I could stay alive." Big Business—more willing

to acknowledge a need for oversight—will settle for reform. Top execs would keep rules that impede smaller competitors while expanding flexibility to choose cheaper compliance methods.

A similar clash is brewing over affirmative action. Small business wants to overturn federal rules they consider complex, costly, and intrusive. Larger companies, better able to absorb compliance costs, want to retain clear guidelines that can be used to protect them from needless bias claims. "Big Business just wants to be left

alone," says Stephen A. Bokart, general counsel for the U.S. Chamber of Commerce.

Despite common complaints about soaring medical costs, small and Big Business differ on solutions. Small companies want reforms to make health insurance cheaper and more accessible by making coverage portable, lifting coverage restrictions on people with preexisting conditions, and helping businesses create insurance-purchasing pools. "You can buy 100 things a lot cheaper than one thing," notes Tom Turner, head of SAS Systems, an Atlanta electronics maker. Corporate America is intent on protecting its existing system, in which nationwide plans are free from varying state regulations. But the two lobbies are more likely to team up on health-care issues than to fight.

TITANIC CLASH? Still, where interests collide, small business can be optimistic. Entrepreneurs often back GOP candidates, while Big Business alienated the Republican minority by siding with Democrats. And small business regularly fought perceived antibusiness initiatives such as Clinton's health plan, while Big Business often cut deals with Democrats to protect individual corporate interests. After the unexpected House takeover, some GOP insurgents say it's payback time. "The knives are out for Big Business because of its willingness to play footsy with Democrats," says Republican pollster Glen Bolger.

What's more, small-business owners dominate the GOP freshman class. And the third-ranking House Republican, Tom DeLay (R-Tex.), owned a small pest-control firm for decades. "We are the party of small business more than Big Business, Main Street more than Wall Street," says Republican National Committee Chairman Haley Barbour.

Already, small business is wielding its newfound clout. Case in point: Gingrich promised to fight efforts to eliminate the Small Business Administration. A GOP leadership aide says Gingrich has told colleagues he has "no interest in taking on small business."

The skirmishes within the business community may be fierce at times, but neither Corporate America nor its smaller rival expects to lose the war on Capitol Hill. Tax cuts of some sort are a virtual certainty, and all businesses likely will win major relief from red tape. Those victories should help salve the occasional intramural wounds suffered on the new GOP playing field.

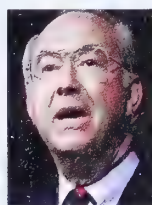
By Richard S. Dunham and Mary Beth Regan in Washington, with bureau reports

Business agenda, it's Main St. vs. Corporate America

LL BUSINESS



FARM SUBSIDIES Favors eliminating subsidies, which House Majority Leader Richard Armey assails as "welfare for the rich."



AFFIRMATIVE ACTION Sees guidelines as a costly infringement of employers' hiring prerogatives. The chief defender: Senator Phil Gramm.



TAXES Favors House Speaker Newt Gingrich's tax agenda, including repeal of 1993 tax hikes on some small companies.

EXPORT PROMOTION Aims to kill off the subsidy program, arguing that corporate beneficiaries—not taxpayers—should foot the bill.



REFORMS

WHY WELFARE REFORM IS SUCH A LONG SHOT

Newt is talking tough, but the political divide is formidable

As the 104th Congress convenes, seething with ferment over the Republicans' Contract With America, no social program seems riper for radical overhaul than the nation's floundering welfare system. GOP legislators, historically hostile to welfare dependency, want tough new eligibility rules and time limits. President Clinton, vowing to fulfill his promise to "end welfare as we know it," is trying to keep pace.

But welfare reform faces an uphill slog. Despite the tough-sounding rhetoric emanating from both Democrats and Republicans, deep ideological differences divide the two camps. It will take astute political navigating to keep welfare revision from meeting the same fate as health-care reform: a collapse into a heap of acrimony.

WAY STATION. Already, the chasm is wide. True, President Clinton and the Republicans both want to convert welfare into a temporary way station that will steer beneficiaries into the workforce. But beyond that, their paths diverge sharply. Democrats, who see the social safety net as a flawed but noble party legacy, want recipients to get job training and seek to cushion their entry into the work world. Republicans want far deeper cuts.

In an attempt to regain the initiative, Clinton is summoning congressional leaders and governors of both parties to a "working session" after his State of the Union address in late January. In the meantime, though, House Speaker Newt Gingrich & Co. have elbowed their way ahead. The new speaker is pressing hard to limit the federal role and is negotiating with governors to make his package more state-friendly.

Moreover, House Ways & Means Committee Chairman Bill Archer (R-Tex.) has scheduled welfare hearings to start on Jan. 13—before Clinton's powwow. The tough tenor of the hearings is presaged in the committee's agenda: welfare and illegitimacy, benefit cutoffs for legal immigrants, and discretionary block grants instead of entitlements.

Both parties are playing to the public's frustrations with high taxes and big government. Aid to Families with Dependent Children—what most peo-

ple commonly refer to as welfare—comprises just 1% of federal spending. Add in food stamps, Medicaid, and other programs, and Washington's spending on the poor still amounts to only 13% of the federal budget. Yet polls show that the public considers welfare a far larger budget problem than it truly is.

Nothing illustrates the parties' strategic differences better than the projected costs of their respective plans: The GOP claims its reforms will save \$40 billion over five years, with \$22 billion coming

from denying legal immigrants access to 60 federal welfare programs. Clinton's plan, unveiled last June, would actually boost spending, by some \$9.5 billion over the same period, to support job training and child-care assistance for welfare moms.

Such numbers reflect other policy differences. The GOP would deny aid permanently to any children born out of wedlock to moms under age 18. By contrast, Clinton's proposal would continue benefits to the underage mother if she lives at home, attends high school, and makes a good-faith effort to establish paternity. And Clinton would pay minimum wage to moms in subsidized jobs; the GOP would simply require recipients to work off their welfare benefits. In such low-benefit states as Mississippi, this would have a welfare mom working 35 hours for \$120 a week, less than minimum wage, says the Washington-based



The Battle Over the Dole

THE CLINTON PLAN

TIME LIMITS Cut off AFDC benefits to mothers 24 or younger after two years unless they get training or a job.

SPENDING Provide \$9.5 billion for such things as job training and child care subsidies to get mothers off welfare and help the working poor.

PENALTIES Reduce benefits to women who refuse to name the fathers of their children, and enforce child-support awards.

THE GOP PLAN

Cut off AFDC benefits to families after two years, and set lifetime limit on AFDC of five years.

Cap spending on many programs for the poor. Convert food and housing programs into a cash grant to the states. Cut some state block grants by 5%.

Deny AFDC and housing benefits to children if mothers are under 18, and use the savings for adoption, orphanages, or homes for unwed moms.

Center for Law & Social Policy, a liberal-research group. The GOP also would have a five-year, lifetime limit on AFDC. While politicians wrangle over such provisions, the future of 5 million families receiving AFDC and the record 27 million Americans getting food stamps is the line. The Health & Human Services Dept. claims Gingrich's plan would cut half of the 9.5 million children on AFDC from the program. Already, the dependency of the early welfare skirmish has alarmed poverty experts. "I don't think the American public is willing to see women and children sleeping under sewer grates," says Judith Gueron, president of Manpower Demonstration Research Corp., which studies welfare programs.

STATES' FIGHTS. Paradoxically, Clinton is looking to Republican governors to help moderate the Contract With America's end. It's the governors, after all, who will be stuck enforcing many of the Contract's radical changes. With so many new Republicans in statehouses, the Clinton Administration hopes the incentives for GOP moderation will increase. Indeed, governors privately worry about the consequences of deep cuts. Both camps agree that "the federal government ought not to mandate a lot of conditions that the states find nearly impossible to meet," an Administration official says. But the Contract With America envisions turning all 15 nutrition programs into block grants to the states and then subtracting 5%. Rather than entitlements—which automatically go to whomever meets the criteria—these programs would become appropriated and subject to yearly budget cuts. That means governors of states with weak economies could be forced to slash welfare spending at precisely the time recipients need the help most.

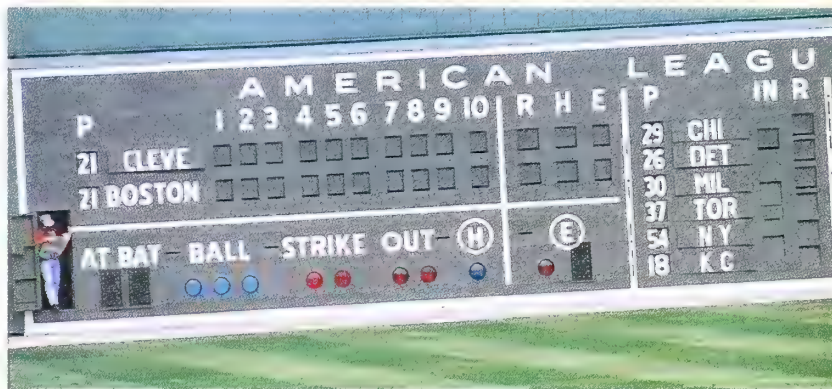
With so much distance between Clinton and the Newtonians, welfare reform faces tough prospects for passage in a highly partisan legislative session. Besides, GOP leaders insist they will tackle congressional reform, tax cuts, and budget-slashing before turning to social reengineering. Even if they can make room on the docket for welfare, and find a sliver of common ground, it's doubtful whether Clinton, an inveterate do-gooder, can bring himself to swallow some of the Republicans' harsher measures. Clinton "will be so happy to have something called 'welfare reform' he will consider almost anything from the Republicans," pretends Douglas Besharov of the conservative American Enterprise Institute. "It's a bet few would put any money on."

By Paul Magnusson and Mike Namee in Washington

BASEBALL: CONGRESS' SURPRISE SQUEEZE PLAY ON THE OWNERS

As the nation's Major League players and owners enter the sixth month of their bitter strike, it's looking more likely that the saviors of a 1995 baseball season may reside on Capitol Hill. Key Congressional Republicans now are threatening to solve the dispute with a dose of one of their favorite elixirs: old-fashioned competition. They're readying legisla-

But Republicans quickly fanned the flames—which is why the legislation is being taken seriously this time. Senate Judiciary Committee Chairman Orrin G. Hatch (R-Utah) has hinted at a bill of his own. While there's only limited sympathy for millionaire players, the pols have even less empathy for the owners, who unilaterally imposed a salary



FENWAY BACK WHEN THERE WAS BASEBALL: Will the GOP ride to the rescue?

tion that finally would end the game's antitrust exemption, a 1922 relic that is viewed more and more as unfair protection for team owners.

No frivolous grandstanding, this. Ending the exemption would enable players to file an antitrust suit against the owners—and perhaps pressure them back to the bargaining table. An antitrust suit filed by players in 1987 against the National Football League eventually helped resolve their labor dispute. If Congress acts, "the likelihood of settlement goes way up," says Donald M. Fehr, executive director of the Major League Baseball Players Assn.

SECOND THOUGHTS. The GOP's threat to rescue the national pastime by taking labor's side is one irony of the Republicans' Nov. 8 election romp. "You'd think unions do best when the Democrats are in control," marvels Brookings Institution economist Henry J. Aaron. In fact, Democrats threw out the first pitch. New York Senator Daniel P. Moynihan, who represents frustrated Mets and Yankees fans, introduced a bill to lift the exemption on Jan. 4. The broad exemption from antitrust laws, which no other American sport enjoys, lets owners divide up exclusive territories for their teams and veto franchise moves.

cap after negotiations collapsed on Dec. 22. "As a baseball fan, I say a curse on all their houses," fumes Senator J. James Exon (D-Neb.). Exon blocked repeal of the exemption on the Senate floor last year but now thinks Congress should step in. **SCARE STORIES.** In the previous Congress, owners overcame attempts to kill the exemption by convincing many lawmakers that exposing baseball to the free market would wreak havoc on the game. And this time around, not all Republicans are rushing in to rescue the Boys of Summer. Senator Arlen Specter of Pennsylvania, for one, still opposes lifting the waiver. He fears that if owners could move their teams at will, his Pittsburgh Pirates might leave town. Others on Capitol Hill worry that increased competition would erode Major League profits, which now support popular but uneconomic farm clubs in many Congressional districts.

In fact, many Republicans are hoping that the mere threat of legislative action might force intransigent team owners to rescue the season. That would give the Republicans a political home run—without actually forcing them to play umpire.

By Catherine Yang in Washington, with Aaron Bernstein in New York



INVESTIGATIONS

MAYBE THEY SHOULD CALL THEM 'SCAMMERS'

Electronic checkout systems may be ripping you off

Hercule Poirot has nothing on Inspector Robert W. Alviene. It's just after Christmas, and Alviene, an official with the Morris County Office of Weights & Measures, is walking the aisles of a Bradlees Inc. store in East Hanover, N.J., dropping items into his shopping cart. He isn't looking for post-Christmas bargains. He wants to know if Bradlees' electronic checkout scanning system is overcharging customers.

Sure enough, for the third time in three months at this store, Alviene finds mistakes at the checkout. A \$21.99 set of bed-sheets scans at \$29.99, and a \$3.99 rawhide dog bone costs 50¢ more than it should. In all, six of the 17 items in his cart have the wrong price in the scanner, resulting in an overcharge of \$12.30 on a \$161.85 total purchase (table). A Bradlees spokesman calls the results "troubling" but denies that the company intentionally tricks anyone. All the same, says Alviene, "the customer is really getting burned in there."

Alviene's shopping trip, expected to produce a fine for the store, is the latest in a nationwide crackdown on scan-

ner overcharges. A Dec. 14 survey by Vermont's attorney general found that local outlets of Ames Department Stores Inc. and Rich's Department Stores had serious errors in their scanning systems. Two days later, Michigan Attorney General Frank J. Kelley announced similar findings at Sears, Roebuck & Co. and Wal-Mart Stores Inc. And J.C. Penney Co. is in settlement talks with San Diego County over its alleged mispricing. The Federal Trade Commission is now work-

CHECKING IT OUT: Scanner mispricing is "a serious national problem"

ing to coordinate the proliferating state and local probes.

Authorities and the retailers say mistakes are a result of human error, not fraud. They say the lapses occur when store clerks fail to enter correct data into scanner computers, especially when prices change. Still, experts believe that the impact, which no one has tallied, is enormous. "It's a serious national problem," says Ken Butcher, weights and measures coordinator at the National Institute of Standards & Technology.

TO ERR IS COMMON. Investigators are focusing on nonfood retailers—such as discounters and department stores—which recently started using scanning technology. Although the technology is capable of 100% accuracy, some stores average as low as 85%, says Butcher. And the mistakes often favor retailers. A California survey of 9,000 items from 300 stores found overcharges on 2% of the products and undercharges on 1.3%. A Michigan study found a 4-to-1 ratio of overpricing to underpricing. "It's one of the few places you can be negligent and make money," says Michigan Assistant Attorney General Frederick Hoffecker.

Retailers staunchly defend the systems, noting that scanners are more accurate than clerks—who punch in the wrong prices about 10% of the time, according to NIST estimates. Some companies also say the issue is being blown out of proportion. "There are a number of individuals around the country who are always looking for ways to achieve instant press, and scanning accuracy seems to be a hot button right now," says a Wal-Mart spokesman.

True, regulators' sampling methods may be skewing their results: By relying

heavily on sale items that have frequent price changes, the surveys suggest an inflated error rate, retailers say. Yet consumer advocates argue that high-volume sale items are where most rip-offs are likely to occur. "If a customer shop-lifts, it's called a crime," gripes Pennsylvania consumer advocate Mary Bach. "But a store can 'shopper-lift,' and it's called a mistake."

To complicate matters, scanners' speed and the disappearance of price tags make it hard to detect errors. "I keep my eye on the prices when they light up after they get scanned," says Carol Hennessey, a 53-year-old office-supply-

Price Check!

Of 17 items audited at a Bradlees store in East Hanover, N.J., scanned prices for six were higher than advertised prices

	ADVERTISED	SCANNED	DIFFERENCE
TIGER TRAIL NAIL TRIMMER	\$6.99	\$7.99	+\$1.00
HARPER'S BEEFHIDE BONE	3.99	4.49	+0.50
FRISKIES FRISBIE RAWHIDE	3.49	3.99	+0.50
ALLISON KEY HOLDER	1.29	2.39	+1.10
PARKER 2" x 2" ADHESIVE	1.49	2.69	+1.20
CRITERION QUEEN SHEET SET	21.99	29.99	+8.00

DATA: MORRIS COUNTY (N.J.), DEPT. OF WEIGHTS & MEASURES

re employee as she waits in line at a supermarket in Morris Plains, N.J. Henssey says she has caught several stores shortchanging her, "but you've got to wonder how many times you don't catch it." To combat pressure from law-enforcement agencies, some retailers have launched programs to improve their scanning systems. As part of a \$985,000 settlement in May with San Diego County,

Kmart Corp. designated a manager in each store nationwide to make sure prices in scanning computers match those advertised. Rich's Department Stores is mulling a similar move. Bradlees charges the correct amount when a mistake is brought to its attention. Some stores go further. Sears, which says it has a 95% accuracy rate, rebates \$5 or 5% off mischarged items, whichever is more. And

Wal-Mart gives a \$3 refund per item. That's scant comfort, however, for customers who think they've been had but can't prove it. For now, keep track of shelf prices, and hold on to your receipts. Inspector Alviene and his cohorts could be coming to a store near you soon.

By Catherine Yang in Washington, with Willy Stern in Morris County, N.J., and bureau reports

COMMENTARY

By Mark Lewyn

THE WRONG WAY TO OPEN THE MEDIA TO MINORITIES

Only in the wacky world of Washington could cable leviathan John C. Malone be deemed disadvantaged. But that's effectively what's happening in a \$2.3 billion deal the Tele-Communications Inc. chief has cooked up with a minority business partner to buy cable-TV systems from Viacom Inc. The transaction, to be announced the week of Jan. 9, allows Malone and his partners to nab coveted cable assets at a deep discount.

Here's how the deal works: Viacom Chairman Sumner M. Redstone will sell his cable systems, with 1.1 million subscribers, to a group of investors led by Frank Washington, a businessman and former Carter Administration official who is African American. Washington will own 21% of the two partnerships set up to buy the systems. The balance will be held by Intermedia Partners IV, a San Francisco-based partnership that is, in turn, 25% owned by Malone's TCI.

PERFECTLY LEGAL. Because Washington retains voting control of the partnerships, Redstone is legally selling to a minority. And under the Federal Communications Commission's Minority Tax Certificate Program, which provides tax incentives to those who sell media properties to minorities, Viacom can defer roughly \$400 million in capital-gains tax it would have had to pay on the sale. Not only that, Malone is only a passive investor. So he'll probably avoid the ire of federal regulators who have nosed around other recent TCI cable deals. If all this seems devilishly clever, that should come as no

surprise: Washington dreamed up the minority-preference program as an FCC official during the Carter years.

Nobody can fault Redstone or Malone for seizing on a perfectly legal loophole. The trouble is that the system permits them to do it. The purpose of the FCC's program is to make it easier for minorities to buy TV properties by offering tax breaks. Broader ownership, the theory goes,

general partner of Intermedia Partners, the transaction may not have happened at all. What's more, Redstone is conducting parallel talks with Malone about dropping an antitrust suit he filed against TCI in late 1993. Malone's participation in the Intermedia deal could hasten that process, though a senior Viacom executive insists these issues aren't linked.

While Redstone admits Malone has a stake in the deal, he says the other partners have far more: "They've got to go out and raise a hell of a lot of money."

Because it's so smart, the Viacom deal may augur more of such arrangements. In auctioning off PCS licenses this April, the FCC plans to give special breaks to small businesses, women, and minorities. The goal is to prevent a spectrum grab by well-heeled companies that could outbid entrepreneurs. But if history is any guide, these preferences will simply encourage big companies to team up with bidders entitled to the breaks.

Indeed, it's all but inevitable: The cost of building a PCS system will run more than \$100 million.

When Congress was run by Democrats, it encouraged special treatment for favored groups. Now the Republicans have a chance to jettison that concept. Such programs may encourage minorities to knock on the FCC's door. But as the price of communications assets escalates, there's likely to be a John Malone standing right behind them.

Lewyn covers communications policy from Washington.



LOOPHOLE: Frank Washington will link up with TCI's Malone

will produce more diverse programming and workforces. The FCC is also applying the program in its awarding of licenses for a new wireless phone service, personal communications services (PCS). But in both industries, the gap between theory and practice should make it a ripe target for the Republican Congress.

Take another look at Viacom's deal. Redstone acknowledges that he would have asked for a higher price if Viacom weren't eligible for a tax break—which comes at the expense of taxpayers. Without the incentive, says Leo J. Hindery Jr., managing

CAESARS: TALK ABOUT A CRAPSHOOT



STRATEGIES

IS RAND ARASKOG ROLLING THE RIGHT DICE?

Caesars Palace may not give ITT an easy entry into gaming

Set back from the bustling Las Vegas Strip, Caesars Palace takes care not to present itself as a joint for the nickel-slot crowd. Its main hall gleams with rows of baccarat tables, where the ante can soar to \$25,000. Big spenders can luxuriate in the Pompeii Suite, replete with sauna and a sound show simulating a volcanic eruption.

Sure enough, Caesars has found itself a high roller—ITT Corp., which announced last month it would pay \$1.7 billion for its Caesars World Inc. parent. The acquisition is the centerpiece of ITT's bid to create an entertainment-and-gambling powerhouse. It follows the company's August agreement to buy half of Madison Square Garden Corp. and its sports teams, as well as a flurry of financial-subsidary sales that together will raise \$3.5 billion this year to help finance the new strategy.

ODD DUCK. The frenzied dealmaking represents a striking coda for ITT Chairman Rand V. Araskog, who, after 15 years of dismantling much of his company's sprawling conglomerate, is set to retire in 1996. But his entry into gambling has been startlingly expensive and risky. Caesars, known in the industry for stodgy management and a risk-averse strategy, may well be the

wrong engine to power ITT's ambitions.

Caesars is an odd duck in the casino crowd: While gambling has moved rapidly toward bigger hotels and family-oriented entertainment, Caesars has stuck to its pursuit of big-time bettors. That's one reason profits have slumped, to pretax margins of 14% in the fiscal year ended July 31: By comparison, margins at Mirage Resorts, which caters to a middle-market crowd, hover around 24%. Indeed, before news of ITT's purchase, Caesars traded at a sharp discount to most of its rivals.

For this, according to Securities & Exchange Commission filings, Araskog raised an initial offer of \$60 a share to \$67.50—when Caesars stock was trading at only \$45. Why? Because he couldn't break into gambling any other way. ITT has struggled for years to join Vegas innkeepers, buying a small parcel in 1989 and three years later taking an 11.5% stake in Bally's Grand. It sold that interest in 1993 and paid \$160 million to buy the faded Desert Inn.

ITT had planned to build a \$750 million, 3,500-room hotel and resort alongside the Desert Inn. But costs skyrocketed, and soon, it began eyeing Caesars instead. Caesars and ITT officials, including Araskog, won't comment. But analysts and

ITT'S VEGAS SCORE

FISCAL YEARS ENDED JULY 31

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AND FIX THAT FLAT BEFORE YOU GO, STANLEY

Goodyear's CEO is buffing up his legacy as retirement looms

Stanley C. Gault has been a miracle worker at Goodyear Tire & Rubber Co. When he arrived as CEO in 1991, after an enviable record at General Electric Co. and Rubbermaid, the troubled company's stock rose in days, and Gault quickly made a name on his reputation as a man who knows both how to market and how to please Wall Street. He cut costs, pushed new products, sold off nontire assets, issued new stock, and ended the choking debt. But Gault's reputation as a man who "came down out of the mountains with all the secrets," as one former Goodyear official puts it, is starting to fray. While the leading U.S. tiremaker is still producing solid earnings gains, its stock plunged 26.5% last year (part), the second-worst performance among the Dow Jones industrials.

Perhaps more damaging, a Gault marketing strategy pushing Goodyear-brand tires into new distribution channels has antagonized independent dealers, prompting at least one lawsuit, and, insiders say, has not produced the hoped-for market-share gains. Gault remains amazed. Last year, he says, "we improved on every front." Still, he needs a quick fix if the misstep is not going to stain his record and pose problems for his unknown successor: Gault, 69, retires at year's end.

STOCK DROP. Like other automotive stocks, Goodyear plunged during 1994 because investors fear higher interest rates will hurt U.S. new-car sales and demand for tires. Rising raw materials prices, meanwhile, are pressing profit margins. Gault says Wall Street hasn't come to appreciate all the progress the company has been making and that U.S. car demand isn't as special as some think, since North American sales of new vehicles account for just 20% of Goodyear's overall revenues. Goodyear, he boasts, last year made more money than all its competitors combined. Analysts estimate last year's earnings at about \$563 million,

up 15% over 1993's return. While he won't make a specific earnings projection, Gault declares: "I don't think we'll disappoint the financial community."

The company's problem with its dealers goes back to 1992, when Gault announced it would start selling Goodyear-brand tires through Sears, Ro-



GAULT: Trying to patch things up with independent dealers

buck & Co., the nation's largest tire retailer. That way, Goodyear could reach customers it never had a chance at, he argued. For Goodyear dealers, many of whom sell Goodyear products exclusively, the move was a blow.

A bigger shock followed in 1993, when Goodyear announced it also would

sell its brand-name tires to Wal-Mart Stores and Discount Tire, a Scottsdale (Ariz.)-based retailer known for its low prices. "It's not the same old Goodyear," declares one big dealer. "I don't think their ultimate goal is to have a win-win situation." In California, four dealers filed a class action in July, alleging that Goodyear's moves diminished the value of their businesses and breached its contracts with them. Says Norman Taylor, a San Diego dealer who is one of those suing: "We have totally lost faith in Goodyear because they were not honest with us."

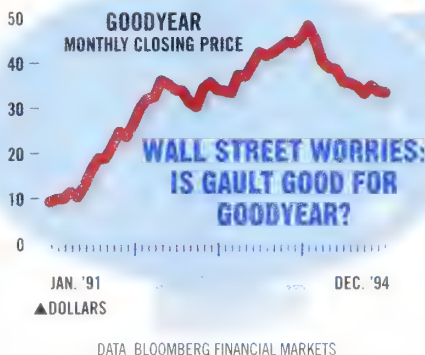
Gault won't discuss the suit but says the new distribution increased car-tire market share for Goodyear's name brand. However, after some initial gains, Goodyear's share has plateaued. *Modern Tire Dealer*, an industry publication, estimates Goodyear's share at 16% in 1994, flat with 1993 and 1 point higher than in 1991. Goodyear disagrees, claiming market share is up 2 points since 1991. Either way, the gain is less than it hoped to achieve.

HAPPY TALK. Gault says the new distribution hasn't hurt dealers as much as some claim but admits that "we probably could have communicated and executed [the distribution moves] more palatably." Now, Executive Vice-President Samir F. Gibara is trying to mollify dealers. Later this month, at a dealer conference in San Diego, he will unveil a program aimed at turning around relations. Goodyear won't describe it, but dealers say it will include exclusive products and a remaking of the sales organization.

Together with another executive vice-president, European chief and manufacturing veteran William J. Sharp, Gibara, an Egyptian-born finance man, is a leading candidate to succeed Gault. A third executive vice-president, Robert W. Tieken, is a long shot, and Gault isn't excluding an outsider. The choice probably will become clear this spring.

Asked if he's concerned that his status as a marketing guru may have lost some luster, Gault replies: "I want all members of the Goodyear family, which certainly includes the Goodyear independent dealer, to be happy and satisfied." And he says he has taken "a close interest" in programs to assure that. Now, he had better hope they work.

By Zachary Schiller in Akron, Ohio



NEW YEAR'S RESOLUTIONS

A HEALTH KICK AT WEIGHT WATCHERS

Boss David Sculley is zeroing in on dieters' physical well-being

Think you have trouble with dieting? Consider David W. Sculley. The trim H.J. Heinz senior vice-president may not look it, but he has been living a sort of dieter's yo-yo in his three years in charge of Weight Watchers International Inc.

The problem: American dieters, a notoriously fickle bunch, in recent years have been taking matters into their own hands—dropping out of diet classes and rushing into health clubs and book stores for fitness and nutrition help. “The whole industry has been under pressure,” says Goldman, Sachs & Co. analyst Nomi Getz. “There has

ers to land on the casualty list, it has had a couple of lean years. The Heinz division predicted it would post \$3.3 billion from class fees and sales of food in 1994—but sales reached just \$1.6 billion. Worse, Weight Watchers went from a \$45 million profit in fiscal 1992 to a \$50 million loss in 1994, analysts figure (chart). And the industry leader admits it has lost 14% of its members during the past two years.

To win them back, Sculley is carving out a health-first, vanity-second message for dieters, who now seem more concerned about heart attacks than love handles. And he will target this mes-

members. And in an attempt to reach out to the long-neglected 5% of the diet world, the company has launched male-only classes. “We don’t want to sit around and talk about makeup and recipes,” says Pittsburgh resident James K. Johnson, 52, who lost 17½ pounds in six weeks on the Weight Watchers’ program. “We’d rather talk about the Steelers game and having a beer.”

Another ingredient in Sculley’s strategy: boosting sales of Weight Watchers food. In December, Heinz acquired All American Gourmet from Philip Morris’ Kraft General Foods for about \$200 million. Adding the brand vaults Heinz to third from fifth place in the \$3.3 billion frozen entrée category, dominated by ConAgra Inc.’s Healthy Choice. Sculley is betting the acquisition will allow Heinz to reach a broader audience.

Rivals are rethinking their strategies, too. Jenny Craig, which closed more than 30 of its 608 franchises in 1994 after earnings plunged to \$1 million from \$59.2 million the year before.

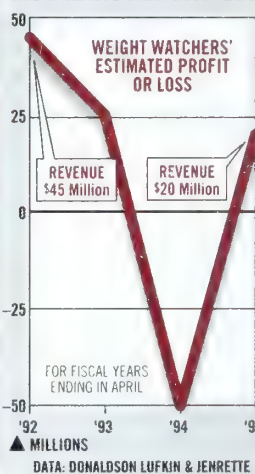
NOT JUST FOR VANITY

Appealing to dieters—men included—who are more concerned about heart attacks than love handles

COUNTING CALORIES IN PITTSBURGH



NOT EXACTLY FAT CITY



been a shift from dieting to general health concerns such as fat intake and general lifestyle.”

To cope, Sculley—kid brother of former Apple Computer Chairman John Sculley—is trying to reshape Weight Watchers with new health-oriented programs meant to appeal to a diverse cross-section of dieters, including men. Timing is critical: The industry’s high season falls between New Year’s and Easter, three months that account for more than half of annual sales. “This diet season will determine the fate of many companies,” predicts John S. Pappas, president of Marketdata Research Inc., which tracks the diet industry.

But one expects Weight Watch-

sage through direct marketing to Weight Watchers’ prodigious database of 11 million former and current customers—a list that competitors Jenny Craig International and Nutri/System Inc. can’t match. “Weight Watchers members don’t think of themselves as former customers,” says Len Tacconi, vice-president of marketing for Weight Watchers. “They think of themselves as being on a break.”

Sculley hopes to shorten the breaks by offering refresher courses that encourage exercise. Stressing the health value of the program, he also has signed deals with insurers such as Independence Blue Cross Inc. of Philadelphia to give rebates on life-insurance premiums to Weight Watchers

will begin TV ads that feature men. And Nutri/System, which emerged from bankruptcy in 1993 under new ownership, has added a personal trainer and weight room to its weekly classes.

So far, Wall Street likes Sculley’s new strategy: Donaldson, Lufkin & Jenrette Securities Corp. is projecting a profit for fiscal 1995 of \$20 million. But the success of Weight Watchers means more to Sculley than to anyone else. If the company does turn around, Heinz insiders say, it could push the 48-year-old Sculley to the front of the pack as the eventual successor to Heinz Chairman Anthony J. F. O’Reilly. You couldn’t ask for more incentive than that.

By Keith L. Alexander
in Pittsburgh

REMEMBER WHEN BRAS WERE FOR BURNING?

For Peggy Anderson, 36, dieting doesn't cut it anymore. And forget regular workouts. "There's no time," says the Chicago-based market-research consultant and mother of two. So Anderson heads to a local lingerie store for extra help—something, say, with a little Lycra. She recently bought a panty girdle and a one-piece "body smoother" to disguise the 15 pounds she would like someday to take off. "If you want to look good in today's clothing," she says, "shapewear is essential."

New name, old idea. Girdles, now spun out of new lightweight, colorful materials such as stretch satin laced with superstrong Lycra, have morphed into the '90s. Retailers from department stores to discounters to lingerie boutiques say shapewear is selling like crazy. In an otherwise lackluster year for apparel, sales of intimate items rose 7.8%, to \$6.5 billion through October, 1994, compared with the year-earlier period, according to NPD Group Inc., a market research firm.

Since 1991, U.S. sales of shapewear alone have risen 12%, to \$350 million, while bra sales have zoomed 17%, to \$2.4 billion, boosted by Sara Lee Corp.'s cleavage-enhancing Wonderbra, which made its U.S. debut last August. "All this Lycra is a sign that gravity is taking its toll on the baby-boom generation," figures retail consultant Alan Millstein. "These are the same women who were burning their bras in the '60s."

TEENYBOPPER BULGE. Demographics and an aging population may explain part of the bulge in foundation-garment sales, but not all of it. Girdles and corsets—once hated for their flesh-constricting features—are turning from avant-garde fashion into mainstream pieces. Designer Karl Lagerfeld presented corsets under suits instead of blouses in his 1994 fall couture showing. And the December issue of *Vogue* featured supermodel Cindy Crawford in a one-piece girdle by Isaac Mizrahi. Retail price: \$645.

Many of the shapewear buyers in Schwartz's Intimate Apparel store, a Wilmette (Ill.) lingerie landmark for 70 years, are teenagers, says store manager Ginny Dack. They're looking for control-top panties and



SPANDEX-ENFORCED CONTROL TOP PANTY HOSE

Battling Baby Boomer Sag

CORSETS Featured in designer Karl Lagerfeld's fall '94 fashion show, corsets are *très chic*.

GIRDLES Prettier and lighter than those of the 1950s and '60s, sales have risen 12% in the past three years.

WAIST CINCHERS Hitting the stores in force this spring, they're large elastic belts designed to reduce the waistline.

CONTROL PANTIES Look like pretty underwear, but do a girdle's work with Lycra panels. Playtex says its Playtex Secrets brand of control panties has become its No. 3 selling brand since it was introduced in 1993.

PUSH-UP BRAS Market researchers NPD Group says the new-style bras, which boost bustlines or keep them from sagging, now account for more than 20% of department-store bra sales.

girdles to wear under prom and graduation outfits. "Young people haven't worn this type of undergarment for years," Dack says. "It's like a new toy for them."

Not that long ago, girdles were more than passé. The feminist movement deemed them Victorian instruments of torture, while fashion designers emphasized a more unstructured, natural look. The advent of control-top pantyhose during the 1970s added the reinforcement for the stomach that many women wanted—but without the girdle's bulk.

LONG-TERM TREND. Times have changed. With more companies relaxing dress codes, fewer women are wearing pantyhose, but they still want the support, says Susan Masko, senior buyer for intimate apparel at Target Stores. And many boomer women aren't content to accept a few bulges just because they're no longer in their twenties.

Retailers say they're pumping up their intimate apparel departments to take advantage of what they see as a long-term trend. For its spring collection, Target is increasing the space it allocates to intimate apparel and boosting the number of items offered. Sears, Roebuck & Co. is doing the same—increasing floor space by "double-digit" percentages in its remodeled stores, says Robert L. Mettler, president of apparel and home furnishings. "It's bust and boom," he says.

This spring, Playtex Apparel Inc., a division of Sara Lee, is rolling out more shapewear offerings: a line of cotton-and-spandex panties that offers control for women who prefer natural fibers. At Target, spring offerings will include body shapers (one-piece garments that go from bust to hip) and thigh trimmers (bike shorts with side control panels). "These aren't grandma's girdles. They're really pretty," says Target's Masko.

That's good news for women, who are likely to see more shape-hugging knit dresses and pants popping up in the stores this spring. And for retailers and manufacturers, who are finding their bottom lines boosted by shapewear.

By Susan Chandler in Chicago, with Ann Therese Palmer in Wilmette, Ill.

EDITED BY KEITH H. HAMMONDS

KRAFT AND GENERAL FOODS BECOME ONE

FOR SIX YEARS, PHILIP MORRIS considered combining Kraft and General Foods, its two big acquisitions of the 1980s—but never took the plunge. Now, finally, it has decided to act, merging the units under the name Kraft Foods. The move gives Kraft a single sales force of 3,500, as well as centralized control over manufacturing. It also eliminates a layer of bureaucracy, cutting 100 jobs. Although a Kraft spokesman denies it, company sources say more heads will have to roll if General Foods' operations move to Kraft's base in Northfield, Ill. The consolida-

tion is Kraft executive James Kilts' first big step since taking over worldwide food operations in December.

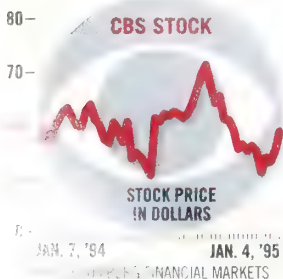
TANDY CLEANS OUT ITS CLOSETS

SLOWLY, TANDY IS FIGURING out what businesses it really wants to be in. First, it got out of computer manufacturing. On Jan. 3, the consumer-electronics retailer said it would close 233 stores in its troubled Video Concepts and McDuff chains. It will also sell its service contracts and most of its credit-card portfolios for about \$760 million. That leaves Tandy to focus on the continuing revitalization of its core Radio Shack outlets and its rapidly expanding Computer City and Incredible Universe chains. As many as 1,400 workers could lose their jobs in the store closures.

CLOSING BELL

AS TISCH TURNS...

Laurence Tisch is keeping observers guessing about his plans for CBS. Last August, the billionaire investor and CBS chairman reduced his stake in the Tiffany Network to 18% after the collapse of a merger with Barry Diller's QVC Network. Now, though, Tisch, who owns his shares through Loews, wants to boost his stake to 25%. Loews will buy CBS stock at an initial price of \$65 per share. Analysts say Tisch's motive may still be to sell out—but at a higher price. If so, his gambit is working: CBS shares rose to 58% on Jan. 4.



MY KINGDOM FOR A 3¢ STAMP

AS OF JAN. 1, THAT OLD 29¢ stamp won't fly anymore—at least, not without a 3¢ stamp beside it. But finding 3¢ stamps isn't easy: Thousands of customers, especially in cities such as Washington and New York, can't get their hands on them. Even when they're in stock, customers complain about long lines. The Postal Service, which printed more than 2 billion of the stamps in anticipation of the rate increase, says it expects the shortage to ease during the next few weeks.

CAREMARK SETTLES WITH JUSTICE

CAREMARK INTERNATIONAL HAS changed its tune. After vowing vindication in court, the home health-care company said on Jan. 3 that it's negotiating a settlement with the

THE POLAR BEAR THAT HAS COKE STEAMING

Those Coca-Cola polar bears sure are cuddly—and Coke's holiday ad campaign, with the bears pushing a Christmas tree up a hill, was one of its most successful in years. It also did wonders for Polar, a \$75 million company in Worcester, Mass., that sells seltzer in New England. A polar bear named Orson has been its mascot since 1902. Hence Polar's cheeky parody, a TV spot launched Dec. 24: As Orson tosses a Coke can in the trash, a tagline pleads: "Keep The Arctic Pure."

Not surprisingly, Coke was quick to take offense,

claiming the spoof was defamatory. A federal judge in Boston agreed, ordering Polar's ad off the air on

Dec. 30. But ever since, Polar has been deluged with letters from loyal seltzer swiggers, many of whom have donated \$1 bills for an Orson defense fund, says

Polar President

Ralph Crowley Jr. Polar execs are plotting a new ad that will poke fun at Coke without defaming it. Meanwhile, the attention hasn't hurt a bit. Says Crowley of his battle with \$14 billion Coke: "We're happy campers."

By Geoffrey Smith



Justice Dept. and the Inspector General of the Health & Human Services Dept., which have long been investigating the company. Caremark was indicted last August for allegedly paying kickbacks in the form of "research grants" to a Minnesota physician who referred patients to Caremark's home-health-care business. Chairman Lance Piccolo says Caremark still could beat the rap, but a lengthy trial would hurt business.

NCR'S CHIEF JUMPS TO LEGENT

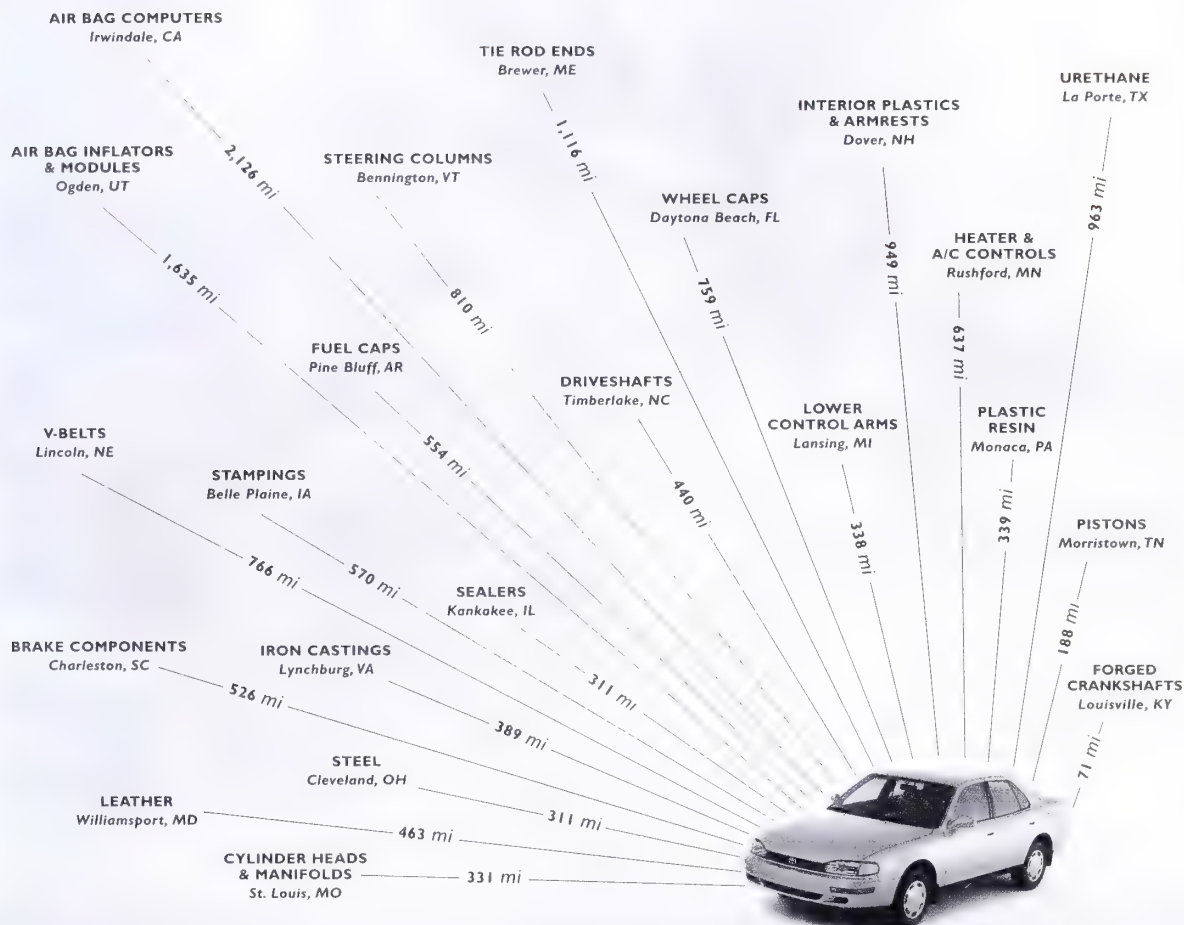
YOU'RE RUNNING A LIMPING computer giant, and someone offers you \$21 million to run a much smaller, much stronger software outfit. Not much of a decision, is it? Jerre Stead, head of AT&T's NCR unit since early 1993, announced on Jan. 3 that he was signing on as chairman and CEO of Legent, a \$500 million software compa-

ny. Known for his kinetic leadership style, Stead had won high marks within AT&T for swiftly downsizing NCR and reorganizing it around customer-focused teams. But the \$7 billion unit, since renamed Global Information Solutions, has not lived up to AT&T's hopes of steady profitability by now. Stead says he found Legent's generous offer, which includes a \$750,000 salary and stock options worth some \$20 million today (but not yet exercisable), difficult to ignore.

ET CETERA...

- Ousted as chairman, ad man Maurice Saatchi will exit the agency he co-founded.
- MCI will charge for its 1-800 directory assistance only with customer authorization.
- IBM Treasurer Frederick Zuckerman unexpectedly announced his retirement.
- Surprise! Eurotunnel is open 24 hours a day, traffic is up, and so is the stock.

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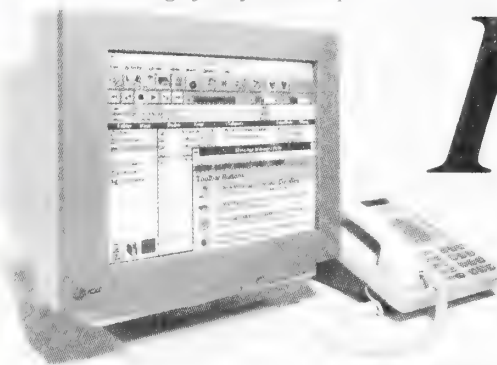
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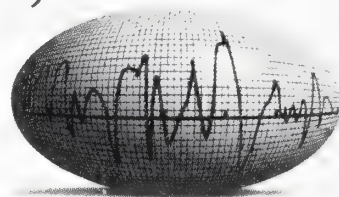
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EDITED BY OWEN ULLMANN

LOOK WHO'S PUSHING FOR MORE REGULATION

Over town, Republican lawmakers are bashing overzealous regulation from the likes of the Food & Drug Administration and the Environmental Protection Agency. But there's a notable exception. As the derivatives mess spreads from companies to local governments, some new GOP lions on Capitol Hill sense they won't appear indifferent to a possible threat to the nation's financial system. So they may lean on regulators to force an industry cleanup. Agencies such as the Securities and Exchange Commission and Commodity Futures Trading Commission already are flexing their muscles against excesses in the derivatives markets. On Dec. 22, the SEC and CFTC settled fraud cases against Bankers Trust New York Corp., which was accused of misleading a corporate customer about the value of its derivatives investments. The SEC recently adopted rules for more disclosure by municipalities that issue public securities, and it's probing the Orange County, Calif., debacle. The CFTC has emphasized it will attack dealers it believes commit fraud.

For some Republicans, more vigilant regulation isn't enough. On Jan. 4, House Banking Committee Chairman James A. Leach (R-Iowa) introduced a bill requiring more disclosure by derivatives dealers and buyers. And Senate



D'AMATO: Seeing Orange

Banking Committee Chairman Alfonse M. D'Amato (R-N. Y.) scheduled Orange County hearings on Jan. 5-6. "Washington can no longer credibly continue to rationalize a laissez-faire approach to derivatives oversight," says Leach.

But political reality will force the Republicans to rely on the agencies to help show Washington's concern. That's because hardly anyone thinks a bill will pass Congress soon.

"LONG SHOT." For one thing, other issues will distract lawmakers. The Contract With America will dominate the first 100 days of the House. And while Leach has been the most vocal champion of the need for action, he will make regulatory consolidation and reform of Depression-era laws separating commercial and investment banking activities his highest priorities. Derivatives legislation this session is "a long shot," says one congressional staffer.

It's not hard to see why. Industry lobbying against such a bill is one problem. So are jurisdictional squabbles between House committees and the sheer complexity of the subject. "You can't pass a law that prevents people from taking the wrong risks," says one executive of a derivatives dealer.

The industry is adopting tougher self-regulatory measures in hopes of deterring Congress from passing legislation. Bankers and Wall Street are drafting codes of conduct for over-the-counter instruments, including derivatives, and the National Association of Securities Dealers is developing sales-practice rules for government securities that include derivative instruments. That may help forestall Congressional action. But it won't stop new GOP leaders from cheering the regulators on.

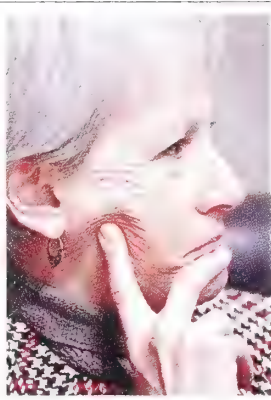
By Amy Barrett

DOING A JOB ON THE JOB CORPS

Senator Nancy L. Kassebaum (R-Kan.), a low-keyed moderate, doesn't usually make waves. Yet the new chairman of the Labor & Human Resources Committee is going after a cherished icon of the Democrats' Great Society: the Job Corps.

Kassebaum plans Jan. 18 hearings on the program, which provides job training and placement for poor, disadvantaged youths. But she has already made up her mind on the thing: The \$1.1 billion budget for the Corps has to be slashed. Kassebaum bases her conclusion on years of Labor Dept. studies. They demonstrate that it costs \$23,000 to train a Corps member, yet only 12% of 60,000 annual enrollees are placed in the craft and vocational jobs they were trained for. Kassebaum insists that Congress should not "perpetuate a program that isn't serving anyone."

Predictably, Democrats are appalled. They contend that the Job Corps has an enviable record, considering that it focuses on youths with bleak job prospects. In testimony to Congress last October, Labor Secretary Robert B. Reich led the program "one of the jewels in the crown of our workforce investment system." His proof? A 12-year-old Mathematica Policy Research Inc. study claiming that 70% of participants go on to a job or more schooling. The study also estimated that the Corps returned \$1.46 for every \$1 in-



KASSEBAUM: Moderate?

vested because graduates paid more taxes and were less dependent on welfare and food stamps than peers who didn't join.

The Clinton Administration—which boosted Corps funding 14% for 1994 and 1995—had plans to expand the program from 113 to 163 centers. Now, the White House must focus on minimizing its losses. Kassebaum alleges that violence in Corps camps is up, living conditions are poor, and dropout rates are high. "It's a very different program from what it was when it started," she says.

Kassebaum prefers to cut funding and reduce violence by screening out applicants with criminal records and imposing a tough code of conduct. If that fails, she'll push to kill the program. That's disheartening liberals, who reckon that if mainstreamer Kassebaum can target the Job Corps with such a vengeance, their hopes of preserving many social programs may be slight, indeed.

By Christina Del Valle

MEXICO: CAN IT COPE?

Zedillo's disappointing plan only makes matters worse

The peso had plummeted, the stock market was on edge, and foreign investors were furious. Everyone wanted to know what Mexico's new President, Ernesto Zedillo Ponce de León, was going to do about the country's currency crisis. So they turned on TVs and radios for a scheduled 6 p.m. Jan. 2 speech and waited for Zedillo to lead them out of trouble. But he never showed. A group of labor and business leaders who for years had given rubber-stamp approval to government economic plans refused to endorse his harsh austerity measures.

When Zedillo finally did appear on television the next day, Mexicans did not like what they heard. The somber President told them to prepare for a year of great sacrifices. "The devaluation will mean a drop in real wages for workers that can only be reversed gradually," he said. In his campaign, he had promised 4% economic growth, a flurry of new jobs, and "well-being for your family." And here he was on TV, offering none of the above.

REVERSAL OF FORTUNE. At the same time, foreign investors were stunned by Zedillo's failure to offer them more than a few privatization crumbs, even though overseas creditors had scrambled to put together an \$18 billion currency-rescue package. As a result, the peso and Mexican markets slid precipitously after the announcement. "His speech was really disappointing, almost shocking in its lack of substance," said one stunned foreign banker. "No one could believe it."

What a change from former President Carlos Salinas de Gortari, who for years had told Mexicans that prosperity was within reach—that they were a First World nation waiting to happen. Zedillo's task was to extend the benefits of hard-won modernization to all Mexicans. But in the past few weeks, Mexicans have seen a shocking reversal of fortune. With the value of their wages slashed, Mexicans' dreams of prosperity have been dashed. At the same time, Mexico has shifted from a sure thing to a risky, developing country in the eyes of foreign investors.

While they will benefit from lower costs, even multinationals are worried about the sudden uncertainty they see in Mexico.

There's a growing feeling of unease north of the border as well—especially in Washington. As the peso tanked, Clinton Administration officials such as Treasury Under Secretary

LEADERSHIP

Zedillo so far seems woefully short on the necessary political skills

**WATCHING THE
PRESIDENT'S SPEECH**



rence H. Summers cancelled ski trips to cobble together global rescue package. Government sources say the Administration may be forced to pony up even more if the first package doesn't work. The peso debacle has once again revived doubts about whether hitching together such different economies as the U.S. and Mexico under North American Free Trade Agreement will ever really off (page 48).

But the biggest concern is the situation in Mexico, where Zedillo has made a disastrous start to what could turn out to be a tumultuous six-year term. Though he served in two Cabinet positions under the charismatic Salinas, Zedillo, 43, doesn't seem to have absorbed his mentor's political skills or knack for projecting an air of authority. The reason Zedillo missed his appointed address was to give business and labor leaders a chance to debate his proposals—something the imperial Salinas would never have allowed. "I don't think their government has shown in any way, shape, or form that they are in control in stabilizing the situation here," says Thomas W. Weisel, CEO of Montgomery Securities, an investment bank in San Francisco.

Despite the market turmoil, many executives and economists believe the underlying economy is basically sound and that devaluation will make investments even more attractive. Years of deregulation and modernization under Salinas

cleaned out the weak players, and Mexico's budget deficit, at 1% of gross national product, is one of the world's smallest.

Zedillo had a chance to redeem himself, but the program he finally produced is technocratic and could be politically unworkable. Its realpolitik is simple: a big squeeze on the domestic economy to keep the powerful forces of global money at bay. The plan calls for price restraint from business and a tight lid on wages to avoid an inflationary spiral. At the

same time it tries to restore investor confidence with an austerity budget aimed at slashing the current account deficit in half, to \$14 billion. Investors are also to be offered a crack at ports, railroads, local phone service, and satellite telecommunications. The main idea is to put a lid on imports and domestic demand while giving the devalued peso time to spark export-led growth.

BIG GULP. Underpinning the plan is the stabilization package paid for by the U.S., Canada, and other industrial countries. Some \$3 billion is to come from international banks including Citicorp and J.P. Morgan. Investment banks are being pressured to help.

After having swallowed huge loan write-offs on Mexican debt in the 1980s, some lenders are not happy about sinking more money into Mexico. But they feel they have to fork over their quota. "If we don't participate, you can be sure we'd be sitting on the sidelines in the future," says one foreign banker. At the same time, however, the banks are feeling queasy because of the big risks involved. If



What a change from the days when Mexicans

were told they were a First World nation just waiting to happen

Zedillo's Rescue Scheme: Will It Work?

PRICE CONTROLS

PROPOSAL

Zedillo is calling for tight wage- and-price restraints to hold down inflation. Companies are to settle for lower profit margins.

RISKS

Price controls will be difficult to enforce. Already, discontented workers are being asked to take a cut in real income.

AUSTERITY MEASURES

Zedillo plans to slash the 1995 budget by \$5 billion and slice the current-account deficit in half, to \$14 billion. He hopes this will restore investor confidence.

He is engineering a recession as growth is expected to fall to 0.5% or less. This will put pressure on domestic banks and weak companies. Mexicans who expected increases in social spending will be disappointed.

RESCUE PACKAGE

Mexico is asking the U.S., Canada, and other governments and international banks for an \$18 billion package to stabilize the peso.

The crisis dents image of the star emerging market. More money could be needed if confidence flags. U.S. commercial banks are unhappy.

PRIVATIZATION

To raise funds, Zedillo wants to open ports, railroads, radio, and satellite telecom to private interests. He may allow sales of Mexican banks and open up petroleum-related sectors.

Proposals may not be aggressive enough to win back massive amounts of cash from abroad. What really interests foreign investors is opening state-run electricity and oil sectors.





INFLATION

Business and labor agreed to measures that should stop a spiral

RETAILERS RELYING ON IMPORTS WILL BE HURT

tion. As manager of the government's privatization of state-run banks two years ago, Ortiz won praise from foreign bankers for his openness and frankness. His chal-

lenge now is to use those same skills to reassure creditors and investors.

Ortiz' mandate is to shift Mexico's source of funding from volatile short-term securities to longer-term investment. For starters, he has turned to Wall Street investment banks to help him design a new series of dollar-denominated notes. They will be offered in exchange for billions of dollars' worth of outstanding *tesobonos*, which are short-term debt instruments sold in dollars but payable in pesos at the current rate. Since the currency crisis began, investors have shown barely any interest in *tesobonos*, even though their yields have shot past 12%. "That's an absurdly low rate in this currency environment," says Bear Stearns & Co. Managing Director Geoffrey E.J. Dennis.

PAYOFF. Investment bankers and money managers think the new notes will have maturities of two to five years and will pay substantially more than U.S. Treasuries—perhaps as much as 20% at the outset. Some fund managers want the notes to be backed by collateral, say a portion of Mexico's oil-export revenues or other hard-currency cash flows.

Ortiz is also expected to move the government toward more borrowing from commercial banks to replace short-term financing by fickle mutual- and pension-fund managers. "The banks can take a longer view on sovereign credits," says Mark J. Siegel, head of emerging markets at Putnam Investment Management in Boston. The banks, however, may be looking at a lucrative payoff. Some Wall Streeters think that J.P. Morgan and Citicorp, among others, will reap hand-

PRIVATIZATION

Sell-offs may expand beyond the skimpy proposal outlined so far

FOR NOW, THE OIL PATCH STAYS OFF-LIMITS TO FOREIGNERS

bying him to allow up to a 30% pass-through of price increases on imported goods to compensate for the peso devaluation. One wonders whether executives will heed his call to trim profits for the good of the country.

Another big question mark facing Zedillo is how willing Mexican workers will be to hold wage increases to 10% or less this year when economists expect inflation of at least 15%. For years, wages have been squeezed to bring down inflation, and today they lag 10% behind 1980 levels. While angry, Benedicto Martínez, a leader of the Authentic Labor Front (FAT), a confederation of independent unions, thinks most workers will see no choice but to go along in a country that is still creating far fewer jobs than the 1 million new workers who come into the market each year. "There's no spirit to fight" when you could lose your job, he says.

Even if business and labor stay in line, Zedillo will need to rebuild his tattered relations with foreign investors, who feel badly burned by the Mexican authorities. One thing he must do immediately is free his talented Cabinet secretaries, so they can use their own, better-honed public-relations skills to stem the crisis. The key man is the new Finance Secretary, Guillermo Ortiz, the replacement for Jaime Serra Puche, who took the for the bungled devalua-

Zedillo doesn't get his act together "the markets will blow right by \$18 billion as if it were a rounding error," says one Western banker.

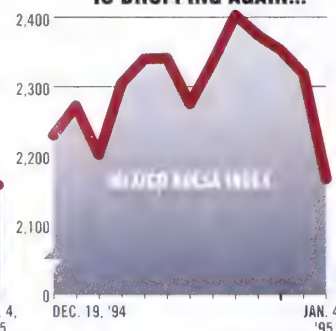
And it's not at all certain that the harried Zedillo can make his plan stick. He is at war with all his main constituencies: Mexican business and labor and foreign investors. Business is lob-

MEXICO'S TROUBLED ECONOMIC LIFE SIGNS

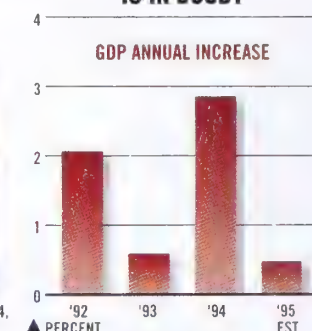
THE PESO HAS RESUMED ITS FALL...



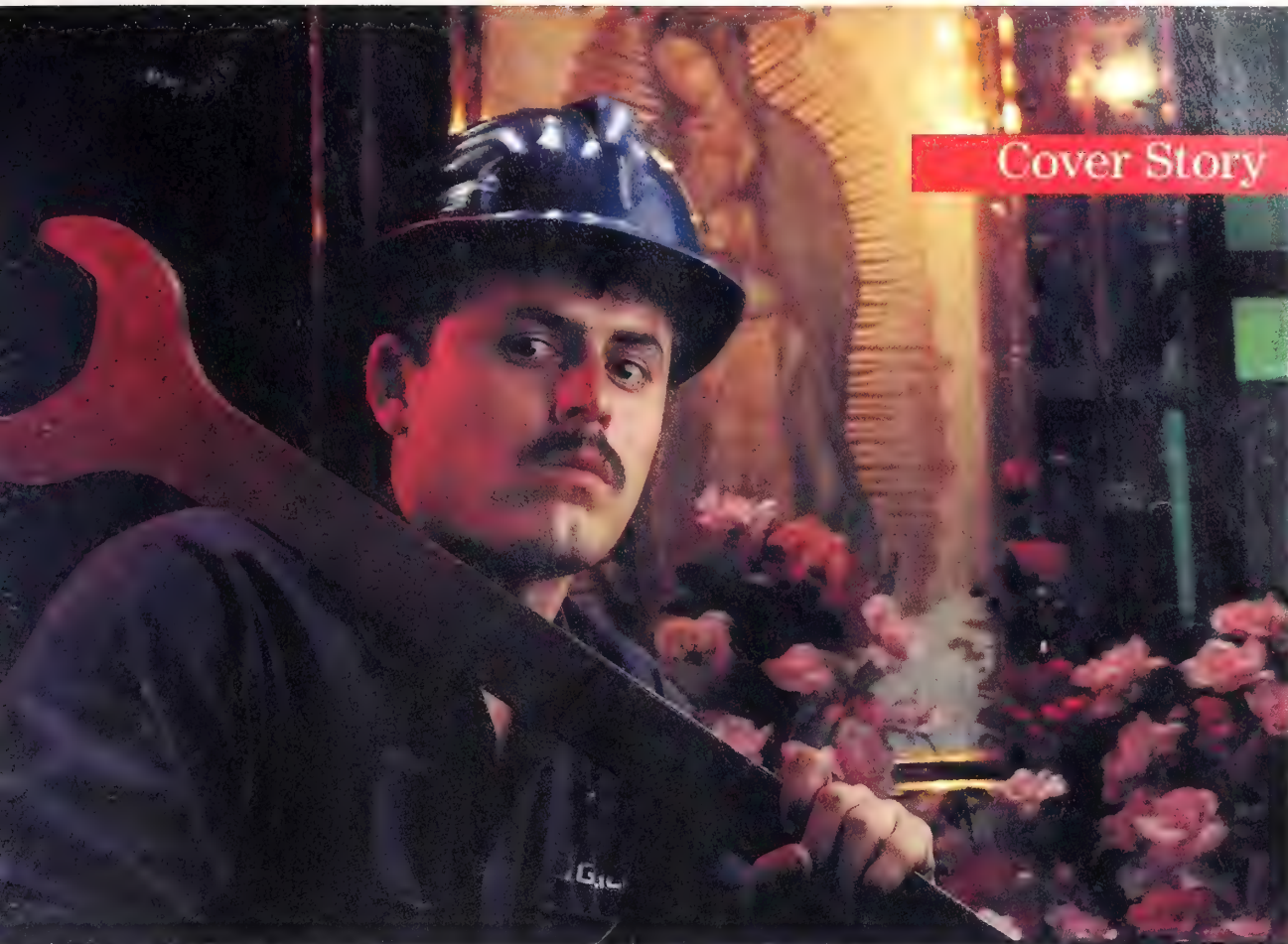
...THE STOCK MARKET IS DROPPING AGAIN...



...AND GROWTH IS IN DOUBT



SOURCE: BLOOMBERG FINANCIAL MARKETS, ORGANIZATION FOR ECONOMIC COOPERATION & DEVELOPMENT, BUSINESS WEEK ESTIMATES



Cover Story

ne profits in coming years by lending Mexico while taking major roles in the new privatization programs.

But Ortiz will probably have to extend privatization beyond the skimpy menu Zedillo provided. Most of what Zedillo offered was already in the pipeline. The one new wrinkle being discussed, allowing 100% ownership of Mexican banks by foreign institutions, which are currently limited to 30%, isn't arousing much interest. Any bank available would probably be riddled with bad loans. But interest is growing in other, more attractive, sectors. Zedillo will come under continued pressure to open up petrochemicals, gasoline marketing, refining and electricity.

Ortiz and Zedillo need to regain the confidence of investors more than Mexico's sake. Because Mexico had been regarded as the Rolls-Royce of emerging markets, any long-term crisis of confidence could prompt investors to abandon developing economies around the world in favor of the safety of the U.S. Already, some analysts are questioning whether equity financing—the cornerstone of many developing markets—will be as available in 1995 as '93 or '94. Indeed, with rising interest rates and a stronger dollar already drawing investors back into America, "a prolonged Mexican crisis could trigger a much broader sell-off," says Paul Sacks, president of New York-based Multinational Strategies Inc. Corporate investors, by contrast, have a longer, more positive view. They're encouraged by Mexico's economic reforms and the solid base NAFTA provides for increased trade. "I don't think our long-term view has changed any," says Vann Buss-

LABOR Will workers really accept a lower living standard when wages are already 10% below 1980 levels?

A METALWORKER: THE COUNTRY STILL CREATES FAR TOO FEW JOBS

mann, corporate economist of Chrysler Corp., which exports minivan engines, Neon subcompacts, and Dodge Ram pickups from Mexico. "For a company like Chrysler, it's a good place to do business."

To Chrysler and others, the devaluation could make Mexico a much more attractive place to manufacture—as long as the cost of local inputs such as labor outweigh the price of imported components. Lower labor costs will "flow right through to the bottom line," says Chrysler President Robert A. Lutz.

One manufacturer thinking of expanding its Mexican operations is Chicago-based R. R. Donnelley & Sons Co., one of the world's largest commercial printers. Senior Vice-President Ronald G. Eidell says several Mexican publishers, which have been printing in the U.S. and shipping back to Mexico, now may take some work to Donnelley's Mexican presses.

ENRAGED. Devaluation could inspire a similar shift in strategy at Dean Foods Co., a dairy and vegetable company in Franklin Park, Ill., that expanded into Mexico recently. CEO Howard M. Dean says the peso's slide has spurred negotiations for a joint-venture manufacturing deal with a Mexican dairy concern. Because of the currency shift, the company is better off making products in Mexico rather than shipping them in from its plants in the southwestern U.S.

If any executive has a right to be miffed at Mexico, it is Charles A. Hayes, CEO of Guilford Mills Inc. The Greensboro (N.C.) textile maker in November closed on a \$15 million purchase of a 75% stake in American Textile, a Mexican producer. "It would have been 40% cheaper if we had done it today," he

PHOTO BY DANIEL F. LEE FOR ENR

says. Still, he remains bullish on Mexico. He figures the cheaper peso will speed the building of an export economy and of a middle class in Mexico.

For that to happen, according to many economists, Zedillo must stabilize the peso and check inflation. Then, "after a period of duress, Mexico can

Cover Story

grow again," says Nora Lustig, an economist specializing in Mexico at Washington's Brookings Institution. "If the crisis can be contained, the fundamentals of the economy can rise to the fore in six months."

Some Mexican executives are already seeing a faint silver lining to the crisis. The devalued currency will protect them from stiff import competition and make their exports more attractive. "This devaluation gives us a competitive edge," says Carlos Slim Helu, whose Grupo Carso conglomerate exports everything from copper tubing to auto parts. Makers of processed foods should benefit immediately, as the cheaper peso makes imports of such U.S. products as Cheez Whiz and Häagen-Dazs ice cream more expensive. Makers of electronics goods, auto parts, and home appliances also will benefit. But for exporters to fully gain the benefits of devaluation, says Juan de la Torre Henson, corporate treasurer for the Mexican auto-parts maker Corporación Industrial San Luis, "many industries still need to improve their quality."

And there is no doubt that there is going to be real pain before a strengthened Mexican economy emerges. Zedillo's planned \$5 billion budget cut will essentially induce a recession. Economists have pared growth forecasts from 4% to near zero for 1995. Slow growth combined with loan rates of over 40% could force many Mexican businesses into bankruptcy. Manufacturers of toys, textiles, and footwear, hard hit by imports, may collapse under the weight of their expensive debt.

"PRETTY ROUGH." Local banks are also vulnerable. In the past 18 months, nonperforming loans have ballooned from 4.5% to an average of 8% of banks' total portfolios, accounting for as much as 60% of their registered capital. Since the peso started collapsing on Dec. 20, interest rates on treasury bills have more than doubled, from 13% to 31%. That has pushed rates for business and consumer loans sky-high. As defaults mount, "banks are going to be hard hit," says analyst Susana Ornelas of Baring Securities Ltd.

Eager to avoid bank failures, Zedillo is planning to draft new regulations allowing foreign banks to take large stakes in Mexican banks—up to 100%. But it is unlikely that many foreign banks, which recently won the right to open their own

subsidiaries in Mexico, would be interested in acquiring troubled Mexican banks unless they were practically given away.

The uncertainty will hurt foreign companies operating in Mexico as well. Fresh from an emergency meeting of the Canadian Chamber of Commerce in Mexico, Douglas Clark, director general of Northern Telecom de México's wireless division, reports that "the next two to three months will be pretty rough." A common problem will be getting paid. Northern Telecom bills its customers in dollars, and Mexican companies are delaying payment. Clark expects a sharp slowdown during the first half of this year. "Right now, our customers don't know what their plans are," he says.

Any foreign company that imports into Mexico is likely to be hurt. The devaluation could crimp American car exports across the border. And retailers, such as Wal-Mart, that depend on imports could find themselves at a disadvantage.



IMMIGRATION If inflation soars and recession hits, the flood of undocumented workers to the U.S. could well surge

A FAMILY WAITING TO CROSS THE BORDER INTO CALIFORNIA

Jay Fitzsimmons, Wal-Mart's vice-president for finance, says the company's plans to open 25 stores with its Mexican partner Cifra this year, could be delayed.

But none of these companies is giving up on Mexico. They aren't happy taking losses, but they will put up with short-term hiccups to reap long-term rewards. Even long-term investors won't stay on board forever, though. If Zedillo's plan unravels, Mexico could enter a downward spiral, producing turmoil and social unrest that could spark a wave of immigration into the U.S.

Zedillo has a tricky task ahead of him. He has to play the tough fiscal administrator to calm the markets and preserve the gains from devaluation. But he also has to convince long-suffering Mexicans that yet another belt-tightening is in their interests. If he succeeds, the last few weeks of chaos will be forgotten, and the hard-working Mexicans and a strengthened Mexican corporate sector could join the North American economy on a more equal footing. In the next few months, we will see whether this harsh early trial has transformed a dour technocrat into a real leader.

By Geri Smith and Elisabeth Malkin in Mexico City, with David Woodruff in Detroit, Stanley Reed and William Glasgall in New York, and bureau reports

By Douglas Harbrecht and Amy Borrus

LIKE IT OR NOT, THE U.S. IS HITCHED TO MEXICO

Searching through the debris of Mexico's crisis, Washington's trade elites can only wince. The debacle, coming just two weeks after the chummy Latin American trade summit in Miami, was more than just a roller-coaster ride for financial markets. The peso's precipitous plunge against the U.S. dollar sent chills through a Clinton Administration that had held up a politically stable and economically growing Mexico as the poster child of its international trade policy.

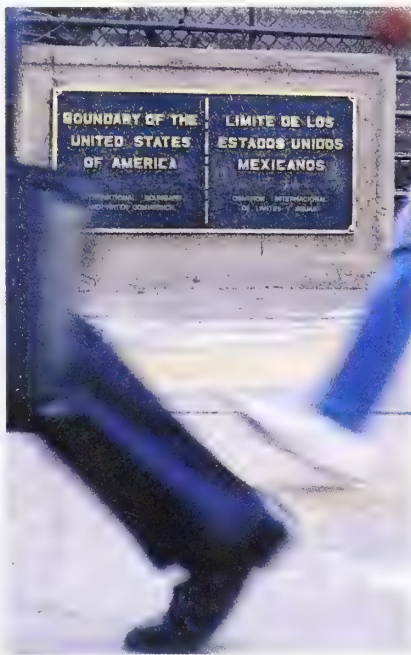
Suddenly, with investor confidence in Mexican President Ernesto Zedillo Ponce de León ebbing, the Clintonites are beginning to fear that their ambitious plan to establish a free-trade zone from Alaska to Argentina could be a pipe dream. The President's much-publicized "win-win" North American Free Trade Agreement, which was supposed to trigger a continental economic boom, is now derided by critics as "lose-lose." Crows AFL-CIO trade expert Mark Anderson: "In my wildest propagandist dreams, I never would have predicted this."

BYE-BYE, SURPLUS. Helping the critics is a stunning setback in U.S.-Mexican trade: Overnight, the 30% devaluation wipes out a U.S. trade surplus with Mexico and creates chronic deficits for the foreseeable future. A merchandise surplus of \$2 billion anticipated for 1994 will turn into a \$3 billion deficit this year, predicts pro-NAFTA economist Gary C. Hufbauer of the Institute for International Economics. Services will suffer the same fate, as U.S. tourists flock across the border to Tijuana and Cancún, while San Diego and El Paso lose free-spending Mexican shoppers.

But there can be no turning away from the U.S. embrace of Mexico. The interests of U.S. government and business are at stake as never before. U.S. exports to Mexico are still an important part of American growth hopes. U.S. banks, retailers, manufacturers, investors, and oil companies all see Mexico as a crucial part of their international strategies. And reviving Mexican prosperity is more politically important than ever at home because of smoldering U.S.

resentment about influxes of new immigrants in key states such as California and Texas.

So even the worst critics of NAFTA seem to recognize that Americans are now united with Mexico in a kind of holy matrimony. The deeper relationship began with the debt crisis of the early 1980s, but now NAFTA has



TIGHT LINK

Washington now
can't afford to
let Mexico crumble

taken it one step further. Mexico's troubles are American troubles in a way that few could have foreseen a year ago.

That helps explain why Washington is moving so forcefully to support the \$18 billion peso-stabilization fund. Big banks such as Citicorp are also part of the movement—because they have to be. Faith in the Americans' own financial system would be damaged if Mexico were allowed to slide into financial chaos. The financial integration has reached the point that senior Administration officials say Clinton will put together yet another stabil-

ization package if this one is depleted.

Yes, there may be a pause in the pace of U.S. direct investment in ambitious new plants, offices, and retail outlets. Wal-Mart Stores Inc., for example, may delay opening some new stores. But few doubt that slowly and methodically, the U.S. business presence in Mexico will continue to expand.

FADING REFRAIN. United Technologies Corp. Chief Executive George David says his company is still looking for small investments of \$5 million to \$10 million apiece. Other major industrial and technological players such as Northern Telecom Inc. and General Electric Co. want to become more deeply involved in Mexico's telecommunications and transportation infrastructures. "We're going to look for opportunities to expand as much as possible," says Ken Brown, chairman and chief executive of GE Mexico. His company's revenues were \$1.4 billion last year.

All of which helps explain why the current wave of Mexico-bashing is

**TIJUANA
CROSSING:
CRITICS OF
FREE TRADE
HAVE MORE
AMMO**

likely to fade. The incoming class of Republican freshmen doesn't share the GOP's traditional free-trade allegiances, and there will be much public posturing. But Clinton will find support for his trade policies from leading GOP moderates such as Senator Richard G. Lugar of Indiana, the second-ranking Republican on the Senate Foreign Relations Committee. "The destiny of the U.S. is to be part of a free-trade hemisphere," says Lugar, who still endorses renewal of Presidential "fast track" authority for negotiating new trade deals without congressional meddling.

Lugar is part of a loose coalition of moderate Republicans and conservative Democrats who represent states and economic interests that are deeply committed to Mexico's long-term success. All of which goes to show that America's relationship with Mexico—like a marriage—is for better or worse.

Harbrecht and Borrus cover international economic policy from Washington.

THE CURRENCY CASUALTY LIST COULD GET A LOT LONGER

Many economists think 1995 could see debt and money crises across the world



When the aftershocks of Federal Reserve interest-rate hikes started rippling through financial markets nearly a year ago, who would have thought that the Mexican peso would eventually become one of the biggest victims of the turbulence? Even after the currency lost more than a third of its value over four brutal December days, many people were still scratching their heads in disbelief. "The reaction of the market has been excessive," International Monetary Fund Managing Director Michel Camdessus insisted to reporters on Jan. 3.

Maybe so. But while the peso collapse is grabbing most of the headlines now, Mexico is hardly the only country whose

currency has become vulnerable to attack. In fact, many economists think 1995 could see debt and currency crises that will make the 1992 European Monetary System blowup look tame by comparison. It's just the latest sign that as global investors become increasingly able to switch from economy to economy at the tap of a computer key, some countries may find themselves getting a drubbing they never anticipated.

What did Mexico in was a mushrooming trade deficit, financed by billions in short-term foreign debt at a time of heavy competition from rising U.S. rates. With an untested President in office for less than a month, all it took was a new flare-up of tensions in Chiapas for foreign investors to start dumping Mexican assets.

COMEDOWN. Now, some other Latin American countries are facing rough going in the wake of Mexico's comedown. Argentina, for example, is grappling with trade deficits of its own. President Carlos Saúl Menem will probably have to enforce a strict austerity program—and maybe even set off a politically unpopular recession—if he wants to continue pegging the Argentine peso to the dollar at a ratio of 1 to 1. One sign of investor concern: Since Mexico's peso troubles began on Dec. 20, the Buenos Aires stock market is off 9%.

But several industrialized countries may also find themselves in the same boat as Argentina. Take Italy. Worries over the collapse of Silvio Berlusconi's government and a national debt exceeding 100% of the gross domestic product are pushing the lira down against the dollar and German

TROUBLE SPOTS IN THE CURRENCY MARKET

ARGENTINA

Inflation is low, but investors are fleeing. To keep interest rates high and preserve the peso's hard link to the dollar, President Menem may trigger a recession.

CANADA

To keep worries about massive deficits from triggering a currency rout, the Bank of Canada will have to keep rates high.

ITALY

The lira is sliding amid concerns over a \$1.2 trillion national debt and political chaos. Some think a debt default is possible.

FRANCE

High unemployment and rising budget deficits are weakening the franc's ties to the German mark.

MEXICO

The peso continues to skid as investors turn thumbs-down to government's rescue plan. Even \$18 billion in international aid may not help.

SPAIN

Central bank is raising rates as political concerns push the peseta to a record low against the German mark. More depreciation is likely.

DATA BUSINESS WEEK

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COULD YOU AFFORD TO LIVE *happen?*





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would true driving*

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as born.



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VOLVO

rk. Some traders worry that
ly may even default on its
2 trillion debt. That could
d investors running for the
ety of U.S. and German gov-
ment debt and touch off a
in reaction of interest-rate
reases, bond defaults, and
rency crises among such oth-
debt-laden countries as Bel-
m, Canada, Sweden, and
ain, where the central bank
sed interest rates Jan. 4 to
end the sagging peseta.

But the risk of financial meltdown in Canada may even be
rse. Like Italy, Canada is burdened by debt and severe
itical ills—in this case Quebec separatism. As a result,
es Martin H. Barnes, managing editor of Montreal's *Bank
dit Analyst*, "investors are demanding a huge risk pre-
am to hold Canadian debt."

TIMES? Yields on long-term government bonds have risen to
despite an inflation rate of 2% or less. But not even
t, or recovery, has stopped the Canadian dollar from slip-
g 5% against the greenback since fall. "Foreign investors
buy Canadian debt, but at an interest rate that keeps
ting worse and worse," warns Barnes. "It's killing us."
France also may fall victim to the currency vigilantes. The
ganization for Economic Cooperation & Development
ects the French economy to expand by 3.1% this year.

THE EDGE

Both Italy and Canada could face financial meltdowns

BARGAIN HUNTERS, OCK AND LOAD

exican stocks will become ever-easier prey

o many stock investors, Mexico had start-
ed to look almost like a First World mar-
ket. American Depositary Receipts in
éfonos de México were the most actively
ded issue on the New York Stock Ex-
ange last year. The Bolsa de Valores was
tively resilient in the face of assassina-
as, peasant uprisings, and a presidential
ction. And ratification of the North Amer-
n Free Trade Agreement made Mexico
m even more like an extension of the good
USA.

Then the peso crisis reminded everyone
t Mexico is still a developing economy.
w, while long-term believers have not
ndoned their faith, even staunch Mexico
ls admit the market will feel the effects of a decimated
rency and shaken confidence for much of 1995. The Bol-
is down 28% in dollar terms since Dec. 16 and may not
e hit bottom. "The market is still not fully discounting
rth-quarter numbers," says Nigel Rendell, James Capel
Co.'s London-based Latin America strategist. "There could
lots of nasty surprises ahead when [companies'] foreign
ot comes out."

For bargain hunters with strong stomachs, one way to
roach the carnage is to look for companies with strong
eign sales and little dollar-denominated debt, since they

But it wouldn't take much to wreck that, especially if Ger-
many's Bundesbank raises interest rates in coming months.

Such a move could force Banque de France Governor
Jean-Claude Trichet into making an unpleasant choice. To
keep the franc in lock-
step with the German
mark, Trichet would
then have to raise
French rates as well. That could imperil France's recovery,
worsen joblessness—which now is a painful 13%—and
swell a budget deficit that is already too large by many
investors' reckoning. But refusing to follow any Bundesbank
rate move would likely end France's efforts to keep the franc
in line with the mark. With upcoming presidential elections
setting traders' nerves on edge, the franc has slipped to a 13-
month low against the mark. "And it's going to get a lot
worse," predicts Mark Turner, managing director of Boston-
based Putnam Investment Management.

It costs a lot these days to maintain a sound currency—
one that keeps inflation at bay, reassures investors, and buys
a flow of imported machine tools and designer duds. To keep
its currency from tanking, a country has to have a gilt-edged
economy and huge reserves of hard cash. With more than \$1
trillion looking for a home in the foreign exchange market
every day, even a slight deviation from the straight and nar-
row can invite a savaging. Mexico discovered this in
December. Now, other countries may find out how bad things
can get when they don't get everything exactly right.

By William Glasgall in New York

are least exposed to the incredible shrinking peso. Using
these criteria, Ricardo Peón at Baring Securities in Mexico
City recommends Industrias Peñoles, which accounts for 11%
of world silver production, and Situr, whose tourism business
should thrive and whose real estate, valued in dollars, is
appreciating by the day. Peón's picks also include Trans-
portación Marítima Mexicana, since shipping will benefit from
rising exports.

What of beloved Telmex? With its ADRs down to \$37, from
\$75 last February, the telecommunications giant looks
attractively valued, says Marianne Bye, Lehman Brothers
Inc.'s telecom analyst. She points out that although the Jan.

3 program announced by the government
suggested a faster schedule for opening the
phone market to competition, "the monopoly
was supposed to expire in August anyway."
So Telmex is no more vulnerable than before
the crisis—just a lot cheaper.

BUY SIGNAL. That's how professional contra-
rians, like Franklin Templeton fund manager
Mark J. Mobius, feel about many Mexican
stocks right now. To Mobius, a market crash is
often a buy signal, and in Mexico's case he is
even looking at companies with severe peso
exposure. "Our feeling is that a lot of the
banks are undervalued," he says. While inves-
tors worry about margins, foreign competi-
tion, and consolidation, he thinks banks such

as Bancomer and Banca Serfin will flourish in the long term.

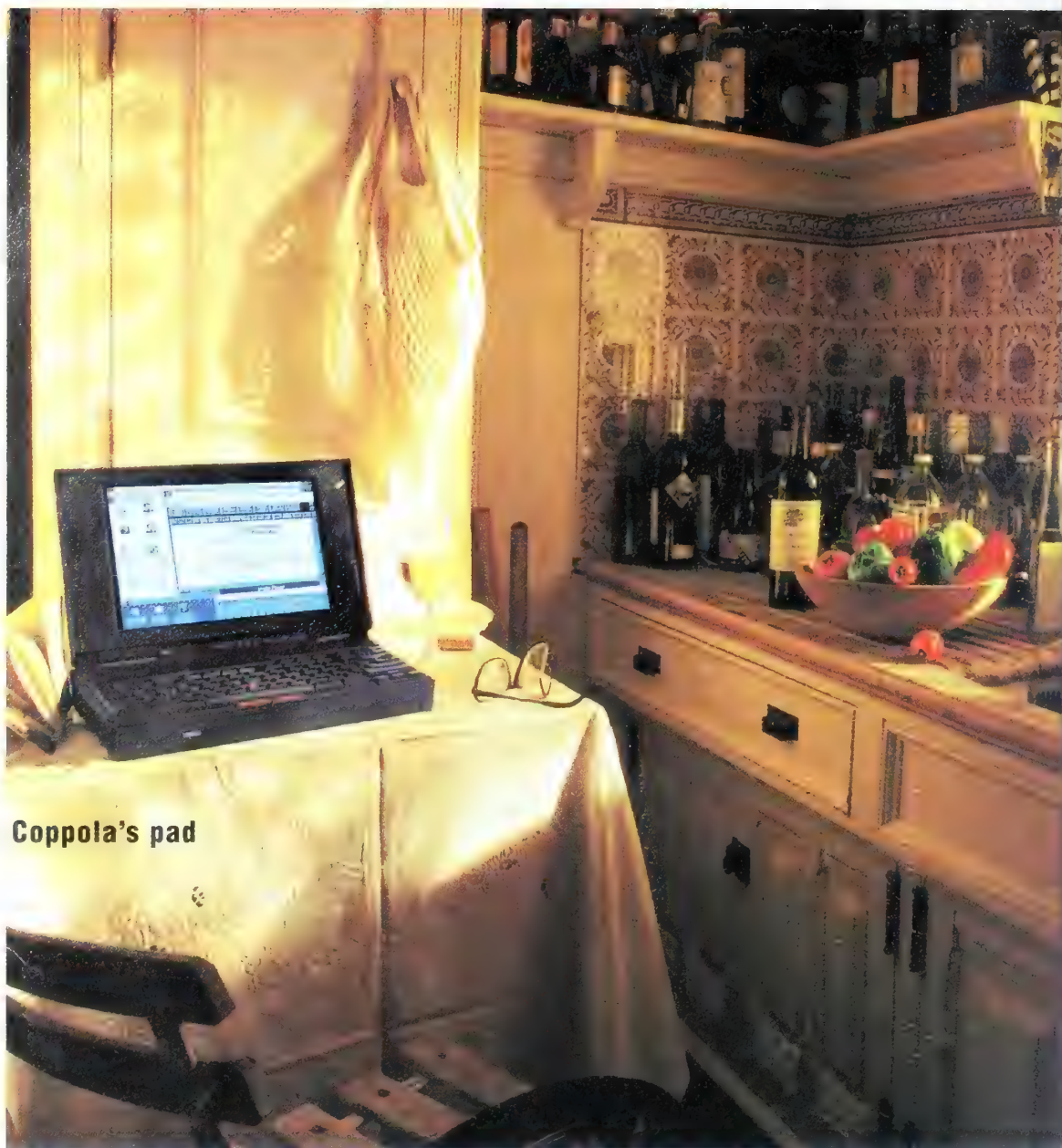
Retail investors seem to want to keep liking Mexico. After
a week of net redemptions in open-end mutual funds that
concentrate on Mexico, money has begun flowing back in,
according to Morningstar Inc.—despite the drop in the funds'
share value. Still, Mexico's low-risk image has been dimmed,
and once its budget details are released and analysts publish
their earnings projections, the Bolsa could give another loud
crash. Just as there's no free lunch, there's no emerging mar-
ket that delivers the rewards without the risks.

By Joan Warner in New York

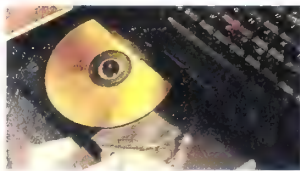
PLAYING THE CRASH

	PRICE ON JAN. 3
GRUPO CARSO (CONGL.)	\$6.44
PENOLES (MINING)	2.61
SITUR (TOURISM)	2.03
TELMEX* (TELECOM)	38.63
TMM*(SHIPPING)	7.00

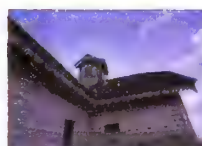
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EDITED BY STANLEY REED

WHO'S PULLING THE STRINGS AT THE KREMLIN?

The effort to crush the separatist movement in Chechnya is fast becoming a debacle for Russian President Boris N. Yeltsin. When Yeltsin gave the green light for the operation on Dec. 11, he was promised that it would last only 40 hours. But more than three weeks later, hundreds of innocent civilians have been slain while fanatical Chechen fighters have turned back several armored assaults on parts of Grozny, the Chechen capital. The army is badly split over the campaign, which will certainly saddle Russia with debilitating economic burdens. There is even a chance that the surge in antiwar feeling could be checked by a return to authoritarian rule, spelling the end of Russian democracy.

The big question is why Chechnya suddenly became so important. After all, Yeltsin tolerated Chechen leader Dzhokhar Dudayev's independence claims for more than three years. One view popular in Moscow blames a hidden power crisis at the Kremlin. October's ruble meltdown was given Yeltsin an excuse to distance himself from Prime Minister Viktor Chernomyrdin, who was starting to emerge as a possible political rival. He has turned instead to old associates in the military and farm sectors. Others think new-found clout include his loyal chief bodyguard, Aleksandr Korzhakov. This former KGB official is also trying to extend his influence: Recently he has lobbied to keep tight state control over oil exports.

In this milieu of intrigue, army advocates suggested a quick war to help stave off big budget cuts, writes economist Vladimir Mau in the liberal newspaper *Sevodnya*. At the same time, other insiders pleaded with Yeltsin to take firm control of oil pipelines in the Caucasus, adds Mau, deputy director of the Institute for Problems of Transitional Economies, a think tank associated with economic reformer Yegor Gaidar. Only that way, the insiders argued, could Russia

guarantee its share of the oil wealth due from big new fields in Central Asia and Azerbaijan.

Now the ill-planned campaign threatens to blow out an unusually tight proposed budget for 1995 that was designed to stem inflation and stabilize the economy. Failure to stick to this plan, which keeps the deficit to 7.8% of gross national product, could cost Russia up to \$15 billion in promised assistance from the International Monetary Fund and other Western agencies. Those budget numbers won't hold if the Chechen campaign continues. Just the cost of rebuilding Chechnya's shattered economy would approach \$690 million.

Moreover, the destruction of Grozny and the bombing of orphanages and private houses is certain to become a Republican rallying cry against U.S. aid in the new GOP-dominated Congress. And the sense of renewed political instability the Chechen adventure is conveying will likely scotch plans for badly needed private investments in Russian companies.

RALLYING CRY. The bloody putsch has already cost Yeltsin much domestic support. Even though Chechens are widely blamed for Russia's big organized crime problem, polls show that the public is disgusted with the bloodletting. Democratic leaders Grigori Yavlinsky and Boris G. Federov have both publicly blasted Yeltsin. Even Gaidar, until now a staunch Yeltsin loyalist, has publicly split with him, leaving the President with the likes of ultranationalist Vladimir V. Zhirinovskiy for allies.

The bigger question for Russia is whether Yeltsin's growing isolation threatens the democracy he risked his life to bring about. He is due to stand for reelection in mid-1996. At this point, many analysts doubt that he will—or if there will even be an election.

By Peter Galuszka, with Geoff Winestock, in Moscow



DO OR DIE: Chechens take to the streets

GLOBAL WRAPUP

HOPE FOR U.S.-CHINA TALKS

With the New Year, U.S.-Chinese relations seemed to take another turn for the worse. U.S. Trade Representative Mickey Kantor threatened to impose \$2.8 billion in tariffs on Chinese imports unless Beijing improves protection of intellectual property rights by early February. China said it would retaliate by excluding U.S. companies from some joint ventures and doubling tariffs on such U.S. consumer goods as cigarettes and cosmetics. Beijing also blames Washing-

ton for blocking its admission to the World Trade Organization.

Yet after sorting through the rhetoric, observers see room for an agreement. Even U.S. officials admit that the Chinese have made progress since 1992 in passing legislation protecting intellectual property rights. "The central government understands the importance [of intellectual property rights] and they believe in it," says a U.S. official in Hong Kong.

Where Beijing has work to do is in convincing many local officials that they shouldn't make knockoffs. For

instance, the U.S. has named 29 factories that crank out illegal CDs. Local government officials often see no benefit in shuttering such industries, which provide jobs and tax revenues.

But as Kantor's Feb. 4 deadline nears, some progress is evident. In early January, the Chinese shuttered three factories in Guangdong province for patent infringements. It will take bigger actions than that to seal a deal. But most China watchers believe both sides desire an agreement to avert an all-out trade war.

By Joyce Barnathan in Hong Kong

**GROVE: NO PLANS TO
OVERHAUL THE CULTURE
HE CREATED**



CHIEF EXECUTIVES

THE EDUCATION OF ANDREW GROVE

Intel has always focused on the next chip. Now, it has to pay attention to consumers, too

Crammed, crowded with management and technical books, and festooned with Post-it notes, Andrew S. Grove's cubicle at Intel Corp. doesn't look much different than those surrounding it. More than anything else at the company, though, it symbolizes the open, proactive culture that has led Intel to sales of \$11.5 billion and absolute dominance of the market for microprocessors—the chips that lie at the heart of the world's millions of personal computers.

Grove sits in a cubicle precisely to eliminate barriers between chief executive and staff. When he is around, anybody can stop by and bend his ear, even

to tell him he screwed up on a decision. There's no fear of getting fired—Grove encourages what he calls “constructive confrontation.” In the ceaseless race to put more transistors on ever-smaller slivers of silicon, there's no time for anything as inefficient as bureaucratic protocol.

Such an atmosphere has propelled Intel to the top of its market and installed Grove as one of the business world's most admired gurus. His two books on management are standard reading in business schools. So why, when news surfaced in late November of a minor flaw in Intel's flagship Pentium chip, did Grove make one of the biggest

blunders of his career by not offering to replace the chips, no questions asked? Because even the best high-tech managers—those most skilled at wringing profits from technological breakthroughs—can be babes in the woods when it comes to selling technology to savvy consumers. And Grove himself, at times, may be more stubborn and less open to criticism than the office architecture suggests.

Much has been made of the notion that Intel's engineers simply couldn't grasp consumers' demands that the Pentiums be replaced. But the problem is really more complicated than that. Sure, Grove is a tightly wound engineer-

Sometimes you need a real jolt to realize a real

PhD who has molded the company in image. But both the secret of his success and the source of his current dilemma is an anxious management philosophy built around the motto "Only the paranoid survive."

Intel is so thoroughly focused on the Herculean task of doubling the number of transistors on its chips every 18 months that it has trouble seeing much else. Its vision is further obscured by a certain macho arrogance born of its market dominance. "The culture, the centralized power, the tremendous profitability—it's a blinding light," says venture capitalist Jack C. Husten, former Intel senior vice-president. Concedes Grove in his crisp Hungarian accent: "Sometimes you need a little jolt to realize a reality that has kind of happened around you. We have to learn the skills that are second nature to others."

HART AND SOUL. Intel's response to the Pentium problem is classic Andy Grove—by turns relentlessly aggressive, coldly analytical, and angrily defensive. He calmly explained that, by Intel's calculations, the problem arises too rarely to concern any but the most demanding scientists. When critics came up with examples of more frequent errors, Grove shot back: "If you know where a meteor will land, you can go there and get hit." He finally acquiesced with a replacement policy, but not until he launched an embarrassing aside: Big Blue announced it would stop selling Pentium PCs after releasing its own test results claiming the chip failed more often than Intel was saying.

While Pentium's Christmas sales and Intel's stock price (chart, page 62) apparently survived the public-relations disaster, the episode shows just how intransigent Intel's culture can be. And it's a good time for that. After years of selling mostly to the business market, PC makers are hell-bent on courting regular consumers. PC sales passed car sales in 1993 and are gaining on those of TVs. Meanwhile, Intel rivals such as Advanced Micro Devices and the Apple-IBM-Motorola consortium developing the PowerPC are mounting credible alternatives to Pentium. And the Apple Macintosh still

has a strong nonbusiness franchise.

Most suppliers of a component leave advertising and marketing to the manufacturer of the finished product. But Grove feels that since the microprocessor is an increasingly integral part of the computer, the company must develop a brand of its own to differentiate itself from its rivals. Its huge "Intel Inside" and Pentium advertising campaigns have thrust the company into the consumer arena. "The microprocessor has become a consumer product," insists Grove. "Its role in con-

Grove's results. With more than 70% of the \$11 billion microprocessor market, Intel's Pentium and 486 chips utterly define IBM-compatible PCs—far more than IBM itself. And the company's 56% gross profit margin is the envy of the industry. That dominance stems directly from Grove's signature combativeness and the culture that has grown up around it. "Andy is the heart and soul of the company," says Chief Operating Officer Craig R. Barrett.

Grove's feistiness has a long history. Born Andras Grof in Budapest in 1936, he was the son of a dairyman who was forced into labor on the Russian front during World War II. The young Grof, who liked to sing opera, fancied becoming a journalist. But when his articles were rejected after a relative was arrested, he decided to pursue science instead. Science was absolute; it couldn't be colored by politics as easily.

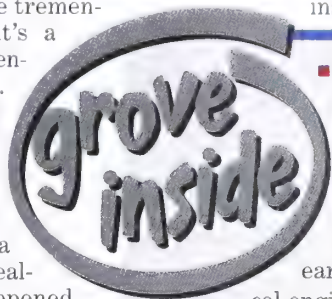
After the 1956 Soviet invasion, Grove left Hungary for New York. He earned degrees in chemical engineering before joining Fairchild Semiconductor in 1963, where Robert N. Noyce had invented the integrated circuit. When Noyce and Gordon E. Moore left Fairchild to found Intel in 1968, Grove joined them as a researcher.

MEMORY LOSS. He made his mark early. In 1971, Grove instituted a late list to note employees arriving after 8 a.m. Outside Intel, he's even more of a heavy. He has spent millions to sue AMD, Cyrix Corp., and others at every turn for alleged copyright and patent violations (although AMD recently won a key decision in the California Supreme Court). He once sent a violin to former White House budget director Richard Darman

to protest the government's "fiddling" with Japan trade policy while the U.S. chip industry burned.

Soon after becoming president and COO in 1979, Grove launched Operation Crush, an all-out campaign to wrest 2,000 new customers away from Motorola Inc. within a year. Intel beat the goal by 500, and one of those customers, IBM, chose Intel's 8088 chip as the brain of its first PC.

But then came the biggest test of Grove's career. By 1985, Japanese chipmakers had driven prices so low that they had crushed their U.S. rivals in the huge market for DRAM memory chips—a technology Intel had invented. Several



■ Born Andras Grof in Budapest, 1936

■ Left Hungary for the U.S. a year after the 1956 Soviet invasion

■ While working as a waiter, earned bachelor's degree in chemical engineering, City College of New York, in 1960, finishing first in his class

■ Received a PhD in chemical engineering from the University of California at Berkeley, in 1963

■ Hired by Fairchild Semiconductor in 1963 as chief of research and development

■ Joined Robert Noyce and Gordon Moore when they left Fairchild to found Intel in 1968

■ Became president and chief operating officer in 1979 and CEO in 1987

■ Teaches management at Stanford University

■ Married for 36 years, two daughters

MOTTO "Only the paranoid survive"

FAVORITE MANAGEMENT GURU Peter Drucker

HOBBIES Tennis, skiing, sailing

ABANDONED TEEN PURSUIT Opera singing

BIGGEST LIE Said he would retire at age 55

temporary society is not a passing phenomenon."

Consequently, many believe Grove is going to have to reexamine his own stubbornly analytical style. In the Pentium debacle, "we shouldn't have taken the arrogant attitude Andy did," says Intel board member Arthur Rock, an initial investor in the company. "He's going to have to change a bit." Says William W. Lattin, a former Intel vice-president and now a top executive at Synopsys Inc.: "Andy's analytical approach is his tremendous strength—and at times a weakness. Not everything with human beings is done with the accuracy of electrons."

Of course, there is no arguing with

kind of happened around you."

other U.S. memory makers eventually ended up in joint ventures with the Japanese. But Grove put his foot down. Over the objection of several executives, he axed the DRAM business and thousands of employees. Unwilling to let the company come to such a pass again, Grove focused Intel on microprocessors with a paranoia and manic competitiveness that informs much of what the company does today.

It comes as no surprise that Intel has never been very effective on the consumer front. As far back as 1972, when the company jumped into the new digital-watch business, it failed to realize it was selling jewelry, not just a timepiece. Then, in 1984, a retail business it launched to sell networking add-ons and modems to PC owners did reasonably well, but never traded its expertise with the rest of Intel. Since 1993, the company has spent some \$100 million to develop and sell a videoconferencing system. But it has yet to fly because it's too expensive. Concedes board member Rock: "It has been terrible on the retail and consumer side."

"DIFFERENT SKILLS." By some accounts, the Pentium debacle is a sign that Grove's vaunted management system isn't as open as it purports to be. True, there was an "all hands" meeting at Intel headquarters five days before the general Pentium replacement guarantee was announced, and Grove says many of the 2,000 employees expressed displeasure with the harsh initial policy. He also received critical E-mail from inside Intel. But his circle of close advisers—about a half dozen vice-presidents—disagreed with the critics, and they held sway.

Indeed, some say Grove is hard to budge once he makes up his mind. "As confrontational as Andy is, there's not a lot of people who can take him on," says Lattin, a Grove admirer, nonetheless. "The people who are intuitive about a market before it develops get driven out." Grove doesn't buy that. "Intuition is not going to get you a 3 million-transistor microprocessor," he growls. "We are fundamentally a technology company. We don't make toothpaste."

True enough, but the company's great challenge will be to keep making the startling technological advances the market takes for granted while learning to track the vagaries of its customers. Grove concedes Intel must change. But he insists it will take incremental adjustment, not a cultural revolution. "Whatever transformation this involves," he says, "it is going to require different skills. Not a different culture."

Critics aren't so sure. A few years ago, Intel tried to better its relations with its manufacturing customers by including their input in the chip-design process. But in 1994, Grove soured things with his biggest customer—Compaq Computer Corp. CEO Eckhard Pfeiffer—by aggressively advertising the Pentium when Compaq chose to push its cheaper 486 machines during the crucial Christmas selling season. The message: Intel's agenda was

more important than Compaq's. "They've had [PC makers] by the short hairs," says management consultant Rich Bader, who ran Intel's small retail operation in Oregon in the mid-1980s. "They treat the consumers with a very similar philosophy."

Some observers suggest that Intel might benefit by recruiting an executive from a consumer company such as Procter & Gamble, at least as a board member. Grove is in no hurry. "I'm not

persuaded that people who come in from a consumer background are necessarily all that equipped for this, either," he says. Besides, he adds, Intel has always worked best by cultivating its own talent; nearly all top Intel executives have worked there at least 15 years. "It's very hard to adopt teenagers into a close-knit family," he says.

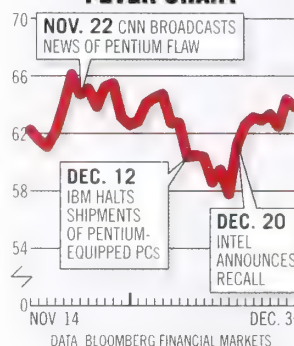
HOT LINE. Grove thinks what Intel needs to do is

open lines of communication to the consumer and analyze the data that flow in. Intel has set up a new hot line to answer Pentium questions, and Grove intends to make it permanent. He also aims to cut through the layers between chip designers and consumers by having engineers regularly staff the hot line, as they have for the past few weeks. Much of the reason the Pentium situation blew up was because customers "flamed" Intel on the Internet. So Grove plans to expand the company's communications in cyberspace as well. "We're going to have tentacles into the PC-buying community that are going to get us closer and closer to the right answers," he says.

Whether that will be enough remains to be seen. But it's a good bet that Grove and his culture will ultimately make a more dramatic response if need be. Grove recalls that when he moved from research to operations at Intel, some people said: "Andy Grove in manufacturing? Ha! Give me a break. And I did pretty well with that." The momentous decision to flee the memory-chip business likewise shows Grove's ability to adapt. Hal Feeney, a former Intel manager who's now a chip analyst at Pathfinder Research Inc. insists that "Andy has made dramatic changes before. He can certainly make them again." Given the growth in home computing, now might be the time.

By Robert D. Hof in Santa Clara, Calif.

CHECKING INTEL'S FEVER CHART



CHIP SHOW: Grove's ad campaigns thrust Intel into the consumer arena

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MUTUAL FUNDS

TENSE SCENES FROM A MARRIAGE

The much ballyhooed Mellon-Dreyfus deal is a resounding culture clash

When Mellon Bank Corp. and Dreyfus Corp. revealed just over a year ago that they would join forces in a \$1.7 billion stock swap, the deal, although it would dilute Mellon's per-share earnings, was heralded as a natural fit and the wave of the future for the banking and mutual-fund industries.

But now, barely four months after Mellon completed the acquisition, the signs of stress in this first big combination of a bank and a mutual fund company are becoming increasingly apparent. While no one is suggesting that the deal will unravel, it's clear that the honeymoon, if there ever was one, is over. And though Dreyfus and Mellon executives still cling to their original vision of the combined company as a financial-services powerhouse for the masses, the day when that will materialize, insiders say, now seems further away that it did just months ago.

SHUNTED ASIDE. Much of the problem is cultural. Mellon had little understanding of the mutual-fund industry, and its bean counting, technocratic culture, sources say, clashes with Dreyfus' lackadaisical management style. That contributed to Dreyfus' lagging behind other major fund groups. Other than cost-cutting, Mellon seems to be offering little direction to Dreyfus, adding to the malaise.

The disquiet has been further exacerbated by the sharp downturn in the mutual-fund business generally. Dreyfus has been losing market share to others, although its decline has slowed in recent months, according to consultants Financial Research Corp. Under pressure to meet optimistic 1995 earnings projec-

“They have all the ingredients ... to make it work. [But do] they have that special gift to make it an overwhelming success?”

— HOWARD STEIN
Dreyfus Corporation



tions and struggling to deal with setbacks at its Boston Co. unit, Mellon, these sources say, is sharply curtailing compensation, spending for new initiatives, and other costs. Some say that could threaten the competitiveness of the combined company.

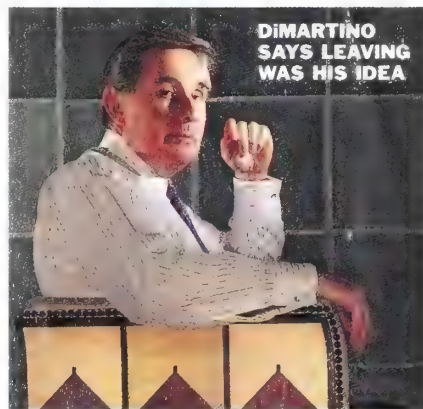
Sources within Dreyfus say Dreyfus chief Howard Stein, who was initially ebullient about the new entity's prospects, has been shunted aside and has

become disillusioned with Mellon's ax-wielding approach to integrating the two companies. Stein would say for the record only that the combined company has “all the ingredients and disciplines to make it work.” But he also questions whether “they have that special gift to make it an overwhelming success.”

Mellon Chairman and Chief Executive Frank V. Cahouet and Vice-Chairman W. Keith Smith, who also serves as Dreyfus' chief operating officer, defend the deal. “There's a great deal of enthusiasm with the direction we've set and the environment that's been created,” says Smith. “We've only owned the company for four months, but what we see of it we really like,” says Cahouet. “The culture fit is very comfortable.”

Some competitors expect Dreyfus to show better results as it makes more use of Mellon's distribution system. The new institution “is something the industry in general is going to have to look out for,” says one rival.

Other observers take issue with Cahouet's assessment, though. “None of



[the culture clash] comes as a surprise," says A. Michael Lipper, president of Lipper Analytical Services Inc. The cultures are "very different." He thinks Mellon "got into the position where they had a lot of money for Dreyfus and are trying to try to drive as much to the bottom line as possible."

D. Says Jay R. DeMartine, Dreyfus' former marketing chief: "The reality is not much of what Mellon has done is necessary. They're bringing greater business discipline. But the skills seem more like the skills of an acquirer than an entrepreneur.... Bankers aren't used to being in the direct marketing business." The most visible signs of upheaval are

gested the idea of changing responsibilities. He says the move was prompted by a desire for a change of "lifestyle" and not by any "dissatisfaction with anything going on in the organization."

On Dec. 30, marketing chief DeMartine, who joined the mutual-fund concern only nine months ago, quit to accept a similar post with the Strong Funds, leaving a critical void in the marketing effort. DeMartine's departure follows closely on the heels of the resignation of Kirk Stumpp, a marketing vice-president for new product development. "The marketing department is the guts of a mutual-fund company," said one Dreyfus source. "It's been decimated." DeMartine de-

ger announcement, mutual funds have been pummeled by rising interest rates, and Dreyfus has been especially hard hit. It has lost about \$10 billion, or 12.5% of its assets, and its market share declined from 3.7% in December, 1993, to 3.1% in October, 1994, according to Financial Research. "We've taken a pretty good sized hit," says DiMartino.

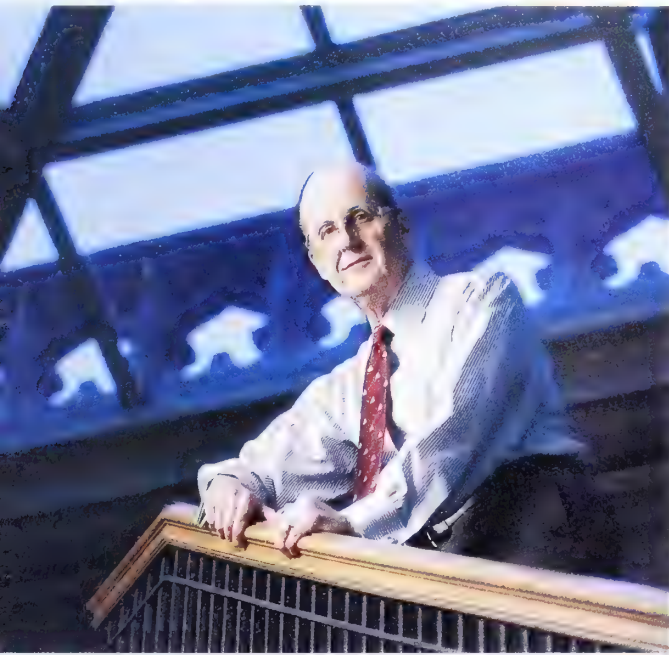
Problems at Mellon's Boston Co. unit, an investment management company that Mellon bought from American Express Co. for \$1.4 billion in May, 1993, are said to be distracting Mellon executives and resources from the task of integrating Dreyfus. In November, Mellon said it would write off \$130 million as a

result of losses on derivatives holdings by Boston Co.'s securities lending business, rather than pass the losses on to clients. Dreyfus sources think these pressures have prompted deeper cuts in spending for business development, compensation, and technological improvements than either company originally contemplated.

Mellon concedes some problems. Last year, Cahouet predicted the Dreyfus acquisition could boost Mellon's earnings by 3% to 6% by 1996. He now says this won't happen because of the impact of rising interest rates on

Dreyfus' fixed income funds. Still, Vice-Chairman Keith Smith expects 1994 earnings to be up about 10% over 1993. As for the merger, says Cahouet, "With a large transaction there are people who feel good about it and people who don't." For now, at least, many at Dreyfus seem to fall into the latter category.

By Phillip L. Zweig with Kelley Holland in New York and Keith Alexander in Pittsburgh



"We've only owned the company for four months, but what we see of it we really like. The culture fit is very comfortable."

— FRANK CAHOUE
Mellon Bank

changes at the top. On Jan. 5, Dreyfus expected to announce that, contrary to the original plan, Dreyfus President Joseph S. DiMartino, 51, had resigned his Dreyfus post and Mellon directorship of Dec. 31. He is expected to be replaced by Mellon's Smith, who had already begun to assume many of DiMartino's duties. DiMartino, who joined Dreyfus in 1971 and became president in 1982, insists that he sug-

gested the idea of changing responsibilities. He says the move was prompted by a desire for a change of "lifestyle" and not by any "dissatisfaction with anything going on in the organization."

gested the idea of changing responsibilities. He says the move was prompted by a desire for a change of "lifestyle" and not by any "dissatisfaction with anything going on in the organization."

Rough Going

Initially heralded as a dream deal, the Mellon-Dreyfus merger has encountered some troublesome snags

The Mellon bean-counting culture is colliding head-on with Dreyfus' informal management style. Some Dreyfus executives question Mellon's emphasis on expense reduction rather than business promotion.

- In a departure from the original game plan, longtime Dreyfus President Joseph DiMartino has resigned to head the Dreyfus fund boards. He is expected to be replaced by Mellon Vice-Chairman Keith Smith.

- Dreyfus chief marketing strategist Jay DeMartine has quit to take the top marketing job at Strong Funds. His departure follows the resignations of numerous other key staffers.

- The Dreyfus funds' market share has declined significantly since the merger announcement. That has caused fees to drop, forcing deeper cost-cutting and slowing progress on certain key projects, sources say.

- Troubles at Mellon's Boston Co., notably a \$130 million write-off on derivatives holdings, has thrown an additional wrench into the deal, adding to pressure on earnings and distracting Mellon executives.

DATA BUSINESS WEEK

INSURANCE

DOWN SO LONG, LOOKS LIKE A SEA CHANGE FOR INSURERS

Property and casualty cycles may be a thing of the past

For almost as long as insurance executives can remember, the \$250 billion property and casualty industry has been locked into recurring—and perverse—cycles. The spells when the world gets a brief respite from calamities—floods, earthquakes, riots, hurricanes—are often tough times for P&C insurers. Low losses make for fat surpluses, which in turn create intense competition and falling rates. On the other hand, when mankind is beset by disasters, losses drain capital from the industry, prices stiffen, and returns rise. “We’re a strange business,” says ITT Hartford Vice-President John Donahue. “If you give us a catastrophe, our stock will probably go up.”

But things don’t seem to be working that way anymore. Since 1991, the industry has weathered more than \$40 billion worth of losses, including such catastrophes as Hurricane Andrew in 1992 and the Northridge (Calif.) earthquake in 1994. And over the past 1½ years, it has been clobbered by a further \$40 billion in pretax losses from the rout in the bond market. But despite these hits, the industry remains stuck in a down cycle now entering its eighth year. The protracted slump, marked by intense price competition in commercial accounts, has even led some industry veterans to declare the cycle dead. “There is no longer, in our view, a property and casualty pricing cycle,” says Alan Levin, managing director at Standard & Poor’s credit-rating agency. **GLUTTED.** Why the change? The industry is awash in capital. During the past decade, the surplus available for paying claims and other expenses increased by more than 10% per year, to \$176 billion, compared with premium growth that averaged only 8% a year, according to estimates by Bernstein Research.

The glut of capital stems from several sources. One was unusually high price



es during the mid-1980s, which attracted both antitrust scrutiny and a surge of eager entrants into the business. Surpluses were also fattened by the bull market in bonds in the early 1990s. All of this has kept the industry’s rate of return well below the rest of Corporate America throughout the past decade (chart). “There’s more insurers than there are needs in some parts of the country,” says George T. Van Gilder, executive vice-president of Chubb Corp.

Don’t expect the pic-

ture to change any time soon. Total premiums increased a paltry 3.9% in 1994, well below the overall growth in the economy and below 1993’s growth level. Business customers are demanding better rates—and getting them. “The whole industry right now is suffering, so the pricing of the really good accounts is getting pretty predatory,” says Rupert Willis, vice-president for standard and commercial accounts at Aetna Life & Casualty.

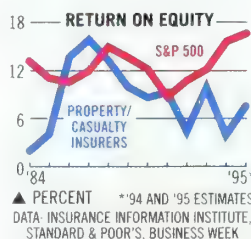
SAFE DRIVING. More than offsetting the impact of catastrophe losses has been a sharp decline in the amounts insurers are paying out in losses on such once-depressed lines as workers’ compensation and automobile insurance. Ratios that measure how much insurers pay in any given claims year compared with their total loss estimates fell to a 10-year low in 1993 for workers’ comp, while ratios in the commercial auto business dropped by 30% from the mid-1980s to the early 1990s. Workers’ comp is benefiting from reforms in state laws and aggressive antifraud campaigns by insurers. And stricter drunk-driving laws, more widespread use of air bags, and a marked decline in the rate of increase in overall medical costs have suddenly made both commercial and personal auto a desirable business. “Auto has been very good for companies,” says Charles A. Bryan, director of property and casualty services group at Ernst & Young. “Right now, that remains a very competitive market.”

Depressed pricing and weak profits have even led to financial troubles at some P&C insurers. Credit-rating agencies have downgraded several major insurers, such as CIGNA and Aetna. These woes have led many of the wounded into rescues by some well-heeled investors in an acquisitive mood. CNA Financial is buying Continental at well below book value, while Home Holdings is in the middle of a controversial recapitalization proposal from Zurich Insurance in which Home would essentially liquidate a good portion of its business while Zurich picks up the choicer renewals.

Although painful, this bloodletting is just what the industry needs to lift itself out of the doldrums. The more weak players leave the industry, the better it will be for the survivors. Of course, a few more world-class hurricanes wouldn’t hurt either.

By Tim Smart
in Hartford

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THE PHANTOM OF ORANGE COUNTY

Little-noticed financial adviser Jeff Leifer is on the hot seat

The great Orange County bankruptcy drama has a cast of thousands. Surrounding the protagonist, former County Treasurer Robert L. Citron, are municipal officials, Wall Street brokers, and lawyers galore.

But so far, one important player has escaped much notice: Citron's financial adviser, Jeffrey Leifer. The head of a tiny Santa Monica (Calif.) firm, Leifer served as Orange County's most important debt adviser in 1993 and 1994 and advised on most of the county's largest municipal-securities offerings. He is among those being investigated by the Securities & Exchange Commission, say sources close to the probe. The SEC wants to know whether Leifer reviewed offering statements to be distributed to investors and adequately disclosed information, particularly about a \$600 million note offering last July. The proceeds of the offering were invested in the Orange County investment pool, which later reported losses of more than \$2 billion. A key question: Did the statement for the notes sufficiently portray the risks of investing in the highly leveraged fund?

Leifer, through a spokesman, denies he had any responsibility for public disclosure and due diligence, claiming that was the responsibility of "other professionals." He is probably referring to Merrill Lynch & Co., the underwriter of the \$600 million issue. The SEC is also investigating Merrill for adequate disclosure. A Merrill spokesman says the firm fully disclosed all risks and is cooperating with the SEC.

OVERSIGHT. Yet some of Leifer's other municipal clients say one of his main jobs was reviewing offering-disclosure documents for financial accuracy. In two cases, they say, Leifer oversaw official statements, which are the municipal equivalent of prospectuses, on behalf of his clients. Rodney Dole, controller for Sonoma County, says that in the five note issues that Leifer advised them on over the past four years, it was "one of his main responsibilities to assist us in preparing the official statement."

James Kenan, director of finance

and administration for the Orange County Transportation Authority, says Leifer was hired in part to review the offering documents: "We were being advised in terms of what needed to be in there—full disclosure in terms of flow of revenue in our case back to 1992."

Leifer began his career at Erlich-Bober & Co., a Los Angeles-based bond house no longer in existence, before joining First Interstate Bank. He worked in its now-defunct public-finance unit and was registered with the SEC as a broker. In 1989, he launched Leifer Capital.

LEIFER CAPITAL'S LINKS TO ORANGE COUNTY

FEBRUARY 1985-MARCH 1989

Leifer works for First Interstate's Public Finance Unit, where he builds contacts in county governments. Launches Leifer Capital in 1989.

DECEMBER 1991

Leifer cultivates Orange County as his biggest customer. Advises on \$117 million in Orange County debt in 1991, 37% of all OC debt issued.

JULY 1994

Orange County issues \$600 million in notes. Merrill Lynch is underwriter, Leifer is financial adviser. By October, Orange County has sold record debt of \$1.3 billion. Leifer is adviser on 73% of it.

DECEMBER 1994

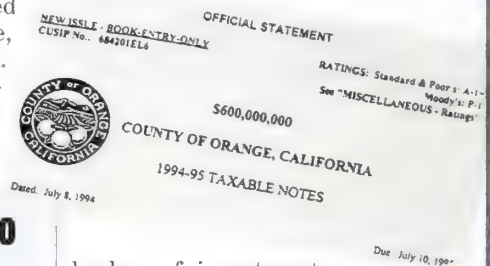
Orange County declares bankruptcy because of huge losses in OC's investment fund. SEC launches investigation into whether risks were adequately disclosed in \$600 million issue by Merrill and Leifer.

DATA: BUSINESS WEEK, SECURITIES DATA CO., CALIFORNIA DEBT ADVISORY COMMISSION

Recently, he hired Ronald S. Rubino, an influential former Orange County budget director. His friendship with Citron blossomed, and Orange County became his biggest customer.

By 1994, he was advising the county on most of its large debt issues. Local officials say Leifer was known for negotiating good prices for his clients and was always available to speak to their gatherings about issuing debt.

DISTANCE. It won't help Leifer that Merrill is busy portraying itself as a mere technician that simply executed a plan Citron and Leifer had masterminded. Merrill is trying to distance itself from Citron and Leifer, despite the giant firm's three roles vis-à-vis Orange County: as underwriter, lender to the investment pool that was run by Citron, and as a



broker of investment products to the fund. "We were never the investment adviser to Citron," says a Merrill spokesman.

What could help Leifer immensely is that the responsibilities of financial advisers are so ill-defined. Such advisers arose in the public sector to act as impartial consultants to bond issuers. Their duties typically include advising municipalities on what form of debt to issue and conducting a search for the best underwriter at the best price.

The bigger issue is that anyone can become a financial adviser. "No regulatory structure touches them at all," says Christopher Taylor, executive director of the Municipal Securities Rule Making Board, a self-regulatory organization that oversees municipal offerings. Leifer Capital, like most independent financial advisers, is not registered with the National Association of Securities Dealers. And courts provide little legal guidance, since most bond-related litigation concerns corporate debt, which doesn't use financial advisers.

With Washington gearing up to focus on Orange County, Leifer's responsibilities—and those of financial advisers in general—are likely to move into the spotlight.

By Nanette Byrnes in Los Angeles with Leah Nathans Spiro in New York



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BY GENE G. MARCIAL

RON PERELMAN: VEGAS OR BUST?

Financier Ron Perelman is known on the Street as a cunning predator. So since he applied for a license to buy a casino in Atlantic City, the betting on which company he is after has been heavy.

Is he out to snare an operator with just a New Jersey presence? Or is the application a first step—as some insist—toward Las Vegas?

Analysts say Atlantic City is the easy route to a Vegas license, since Nevada's gaming commission looks favorably on those who already own one there.

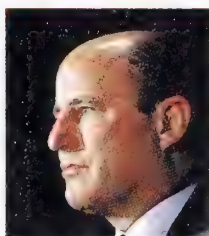
Several highly visible Las Vegas companies are rumored to be Perelman targets, including Hilton Hotels, which owns five Nevada casino-hotels and several regular hotels, such as New York's Waldorf-Astoria. But Hilton's \$1 billion debt and steep market valuation, they argue, might be a turn-off for Perelman, chairman and controlling shareholder of Revlon and Marvel Entertainment Group.

In fact, whisper several Vegas insiders, Circus Circus Enterprises (CIR) is No. 1 on Perelman's list: Its market valuation is among the lowest in the group, based on strong cash flow, mod-

shine its peers. "Moreover, the company has the highest operating margins in the industry for a company its size," notes analyst Dan Davila of J.W. Charles Securities, who believes Circus Circus is likely to be the next gaming company bought out after Caesars World—which ITT has agreed to acquire. Davila puts the takeover value of Circus at 35. Perelman declined comment.

Perelman isn't the only party eyeing Circus Circus, one buyout pro says. Financier Marvin Davis and a group including Richard Rainwater are also rumored to have expressed interest. He says both outfits have talked informally with Circus. Circus Chief Financial Officer Daniel Copp declined comment.

"It is clear," says Oppenheimer's Steve Eisenberg, that Perelman—like Davis, who recently got a license for both Atlantic City and Las Vegas—"is now looking at gaming in a much different light." Eisenberg ranks Circus Circus among the most attractive takeover bets. When savvy entrepreneurs such as Perelman and Davis "go under the hot lights to apply for a gaming license," Eisenberg says, it means the industry is on the threshold of an important new stage.



FIRST STOP:
Atlantic City

line could enhance the Equifax bottom line. "It gives Equifax a larger share of the booming information business," says Jack Sullivan of the San Francisco firm of Harris, Bretall, Sullivan & Smith, which manages \$3 billion. "So we decided to put \$50 million in Equifax," he says.

One Equifax insider estimates that this health-care venture alone could contribute about \$300 million in revenues by 1996. In 1994, Equifax sales hit an estimated \$1.4 billion, with earnings rising to about \$1.60 a share, up from 1993's 85¢. In 1995, revenues are expected to climb to \$1.5 billion, producing earnings of \$1.82 a share.

WHAT MAY HEAL ORGANOGENESIS

As far as short-sellers are concerned, Organogenesis (ORG) is on the brink of financial disaster. The biotech company, they note, has been awash in red ink for years. Yet its shares have been on a tear—shooting from 11 in August to nearly 20. Why?

Organogenesis, which produces material derived from living tissue to replace damaged or diseased skin, arteries, and ligaments, may yet prove the bears wrong, says a New York money manager. He believes a major European pharmaceutical company is negotiating to buy 20% of Organogenesis at 20 a share, in exchange for an exclusive marketing agreement for Organogenesis products. The Europeans will also fork over \$25 million as part of the agreement.

A key product is Graftskin, designed to help those patients suffering from pressure sores, diabetic foot ulcers, and venous leg ulcers, according to Dr. Gerit Mulder, director of clinical and regulatory affairs at Organogenesis. The company has approval to market Graftskin in Sweden and has applied for similar rights in 20 other countries in Europe and Asia, says Jim Trozze, director of research at Moors & Cabot, an investment firm in Boston. Graftskin studies have been completed in the U.S. with favorable results, he says. So the company will seek approval from the Food & Drug Administration this year, says Trozze.

Despite the shorts' claim, says Trozze, Organogenesis "is a long-term investment in the future of replacement skin that addresses vast markets worldwide."

THE PERFORMANCE TO WATCH



est price-earnings ratio, and massive holdings: eight Las Vegas gaming properties, totaling 13,660 hotel rooms and 596,000 square feet of casino space. Trading at 24, the shares sell at a 20% discount to the group's average price ratio. And Circus' debt is less than half its capitalization. Its return on average equity, about 24%, and its project-return on assets, nearly 10%, out-

EQUIFAX EYEBALLS MEDICAL RECORDS

Equifax (EFX) is big in the controversial but profitable business of providing businesses with consumer data for credit evaluation and insurance claims. Now, it's expanding into another lucrative field: supplying medical records and data about doctors to outfits such as HMOs and hospitals.

Equifax already helps determine applicants' risk categories for life and health insurance. Now, according to one money manager, it will provide health-care providers and insurers with hitherto-unavailable data on the ailment patterns among groups of people. The market for such information "will be huge, given the government's vow to cut health-care costs all around," says an Equifax insider.

Some pros say this yet-unexploited

A photograph of a computer monitor on a desk. The monitor is dark and has a red text overlay. The text reads: "Say goodbye to working in an isolation chamber." The background is a light, hazy gradient. The monitor is on a dark desk, and a keyboard is partially visible in the bottom right corner.

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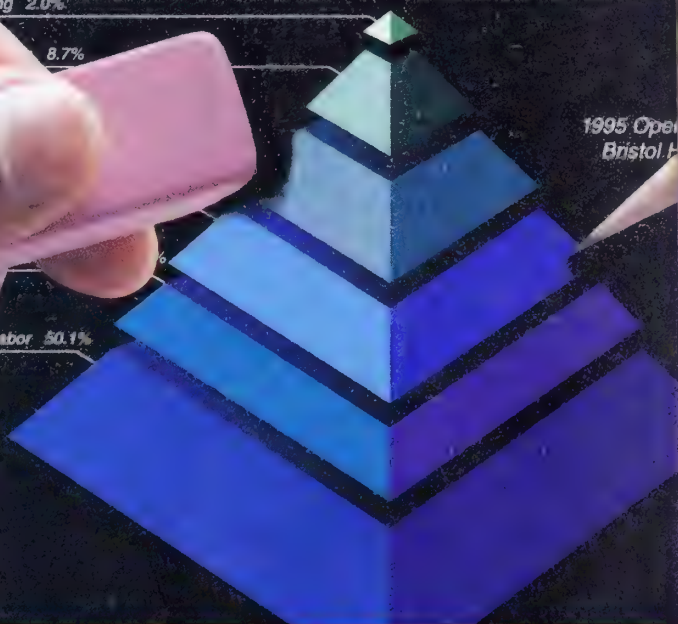
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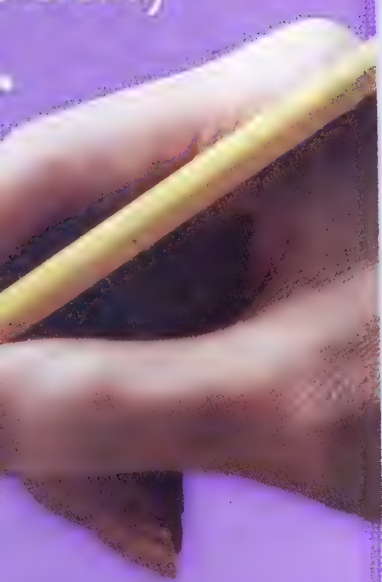
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WHAT THE YIELD CURVE IS TELLING US

Most economists say its message is slow growth ahead

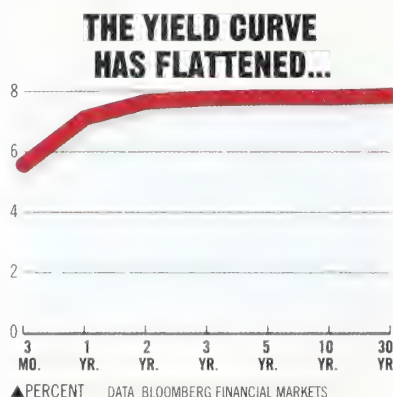
Rarely do economists insist they have a foolproof method for predicting future economic activity, but these days more and more prognosticators are putting their faith in the signals being sent by the yield curve—a simple, connect-the-dots rendering of where interest rates are along the maturity spectrum from 3-month Treasury bills to 30-year Treasury bonds. Trouble is, much like a Rorschach test, different people looking at the same curve come up with different economic forecasts. Some believe the yield curve is saying growth will slow down in the second half. Others believe it's predicting a sharp slowdown or even recession by early 1996. And an academic who did extensive yield-curve analysis in the 1980s says the curve is telling him that growth will be fairly strong in 1995.

Disagreement comes over the significance of one incontrovertible fact—that the yield curve has been flattening lately. That means short- and medium-term interest rates have been moving higher, while long-term rates have been steady. Historically, such a flattening of the curve has predicted slower growth, while an inversion of rates—when short-term rates move above long-term rates—has signaled a recession to come.

HISTORY LESSON. In mid-December, the rate on the 5-year Treasury note climbed above the rate on 10-year bonds, and it has remained at or close to the rate on 10-year instruments since then. And while the 3-month and 6-month rates remain well below long-term levels, they nonetheless have been rising thanks to market pressure and action by the Federal Reserve Board. Moreover, the spread between the 1-year rate and the 10-year rate has been narrowing lately. It may be difficult for anyone but yield-curve aficionados to recollect such shifting relationships between rates and what they presage, but one case may jog people's memories: In 1980, short rates shot way past long rates and touched 20% for a time. A deep recession ensued.

Technically, only one segment of the yield curve—the 5- to 10-year stretch—

inverted last month. But that's enough for David H. Resler, economist at Nomura Securities International Inc. That inversion tells him that "we're headed for significantly slower economic growth in the second half" on the order of about 1½% or so, vs. 4% for the second half of 1994. Historically, he says, an inversion in the middle segment of the yield curve has always signaled slower growth about six months down the road. And,



...RAISING THE CHANCES OF A RECESSION

The inverted yield curve has predicted the last five recessions

DATE WHEN 1-YEAR RATE FIRST EXCEEDS 10-YEAR RATE	LENGTH OF TIME UNTIL START OF NEXT RECESSION
Apr. '68	20 months (Dec. '69)
Mar. '73	8 months (Nov. '73)
Sept. '78	16 months (Jan. '80)
Sept. '80	10 months (July '81)
Feb. '89	17 months (July '90)

DATA: FEDERAL RESERVE

he adds, it generally signals a recession or growth recession—very slow growth after a period of robust growth—18 months after that inversion.

The theory behind yield-curve analysis is a simple one. Interest rates reflect the price of money, and in so doing, they convey information about people's expectations about growth and inflation and their preferences about holding money. Thus when long rates are rising

faster than short rates and the yield curve has a positive slope, people are expecting strong growth and higher inflation and are demanding higher interest rates on longer-dated securities. When short rates rise faster than long rates and the curve flattens or inverts that means they expect weaker growth or recession and lower inflation, so they accept lower rates on long-term bonds.

Thus it's logical, says Campbell R. Harvey, a professor at Duke University's Fuqua School of Business, that inverted yield curves are clear "omens" of recession. Harvey, in his doctoral dissertation, studied the relationship between 3-month and 10-year Treasury rates over several decades. He found that since 1955, an inversion of these rates produced, with a 5-quarter lag, a recession whose duration generally matched the length of the inversion.

There was only one false signal in the mid-1960s. But the Fed was manipulating the yield curve to support the dollar then, and even so, the inversion did precede what was widely deemed to be a "growth recession." Mark Zandi, economist at Regional Financial Associates Inc., says that without heavy government spending at the time, there likely would have been a recession in 1967, as the inversion in 1966 predicted. **TILT?** What happens next depends on whether or not today's flattened yield curve tilts over and truly inverts across the maturity spectrum. Katherine R. Hensel, chief investment strategist at Lehman Brothers Inc., looked at the relationship between 1-year and 10-year Treasuries and found that the curve was similarly flat in the early 1960s and in 1971, 1975, 1977, 1984, and 1986. Not all these periods were followed by a yield-curve inversion and recession.

Other analysts also are expecting slow growth, but not recession. RFA's Zandi figures the shape of the yield curve points toward 2% growth in the second half of 1995. But Harvey is counting on only a slight moderation in the growth rate, to about 3½% to 3¾% by yearend. That's because he doesn't think short rates have moved high enough to slow growth that much. And he isn't looking for a true inversion of short rates vs. long rates anytime soon.

The yield-curve watchers may not always agree on exactly what the flattening of the yield curve means, but all of them, including Harvey, agree on one thing—if short rates rise above long rates, recession is sure to follow. No Rorschach test will be necessary to divine what kind of damage that will do.

By Karen Pennar in New York

If you're age 40, and want to enjoy your retirement, you've reached this page just in time.

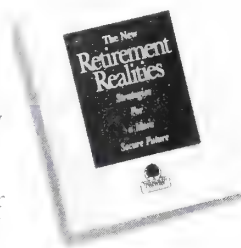
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Showed Up Late,
Never Taken A
Vacation Or A
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Corporation

STRATEGIES

EDGAR JR.'S NOT SO EXCELLENT VENTURES

Moves by Seagram's new CEO are playing to mixed review

Soon after taking over as CEO of Seagram Co. last June, Edgar Bronfman Jr. went to Toronto to meet with analysts. But if the 39-year-old scion of the Bronfman family expected a grace period, he got a grilling instead. The analysts peppered Bronfman with questions about his acquisition of a 14.9% stake in Time Warner Inc., the poorly performing media giant. Asked one pointedly: "Is it true you just wanted to have dinner with movie stars and you spent \$2 billion to do it?" But the onetime Hollywood movie-maker brushed off critics: "I'm not going down in history as the one Bronfman who pissed away the family fortune."

Bronfman comes from a long line of people who take the family fortune seriously. The family still owns some 36.4% of Seagram's stock. But seven months after succeeding his father, Edgar Sr., as head of the Montreal-based conglomerate, Bronfman is still struggling to establish a name for himself. Although groomed for the top since joining Seagram over a decade ago, Bronfman—who spent his twenties writing pop songs and producing a series of forgettable movies—has never fully shed a reputation as a dilettante who owes his job more to nepotism than to business acumen.



BRONFMAN: When will his Time Warner stake pay off?

Bronfman declined *BUSINESS WEEK* request for an interview. But company executives and industry sources say the new CEO is determined to make his mark by spearheading an ambitious acquisitions program that is pushing the spirits giant well beyond its traditional liquor business. Faced with declining alcohol consumption, Bronfman is reshaping Seagram into a more broad-

d beverage and media company. But
ar, his moves have played to mixed
ews. "Edgar Jr. [wants] to make
ram a full-line beverage company,"
Tom Pirko, a consultant who runs
mark Inc. "But the seminal issue is
re is the company going?"

iversification isn't new for Seagram.
1981, Bronfman's father acquired a
% stake in DuPont Co. Ever since,
chemical giant has provided the froth
Seagram's earnings, while Seagram's
r business has generated sluggish
ns compared with global rivals. An-
Irene Nattel of BZW Canada Ltd.
cts Seagram's net profits before non-
rring items for the year ending Jan.
o rise 35%, to \$876 million, on a 4%
ase in sales, to \$6.3 billion. DuPont
ld account for 72% of those profits.
ronfman has argued that Time War-
is a similar long-term investment
will allow Seagram to profit from
th in entertainment. But so far, with
cing costs on the shares exceeding
dividends, Time Warner is hurting
ottom line. And since May, 1993,
n Seagram announced the stake,
Warner's stock has barely moved.

SCALE SHIFT. Many on Wall Street
ve that Bronfman eventually wants
ay a more active role at Time War-
But while Seagram could profit from
rnaround at the media giant, the
e has drawn sharp criticism from
holders. "If I wanted to own Time
ner, I'd buy it myself," says Scott
man, vice-president of equities at In-
ors Group Inc. in Winnipeg, Man.,
h owns 2.4 million shares of Sea-
stock. Adds Bill Newbury, an ana-
at College Retirement Equities,
h owns 664,000 shares of Seagram:
is Edgar Jr.'s first big venture,
I have to say that caution is war-
ed." Seagram's stock, which traded
nd 30 in May, 1993, trades in the
e range today.

ronfman's efforts to diversify in bev-
es have also brought mixed results.
ssen Seagram's dependence on alco-
he bought the tiny maker of Soho
ral sodas, for \$14 million in 1988. It
later sold for just \$2 million. Next
ought juicemaker Tropicana from
rice Co. for \$1.2 billion, and later in
e, he paid \$850 million for Martell
nagac to strengthen the portfolio of
mium alcohols. In 1993, Bronfman
ired distribution rights for Swe-
Absolut vodka.

dustry sources say that in his zest to
rands, Bronfman overspent. He paid
mes earnings for Martell and a huge
mium for Tropicana: The \$1.2 billion
tag was well over the \$800 million
icana managers were offering for
company. "Seagram always pays a
f money," says Pirko. "You should al-

Despite Pricey Acquisitions...

• Paid \$14 million for maker of Soho Natural sodas in 1988. Sold for \$2 million in 1991.

• Bought Tropicana for \$1.2 billion in 1988. Returns have been well below Seagram's expectations.

• Bought Martell Cognac for \$850 million in 1988. Analysts say price for the premium brand was steep.

• Acquired 14.9% stake in Time Warner for \$2 billion in 1993. Stock has remained virtually flat.

• Acquired distribution rights to Absolut Vodka in 1993.

...DuPont Still Fuels Seagram's Growth

PRETAX EARNINGS (MILLIONS)	FY 1995*	FY 1992
SPIRITS AND WINE	\$695	\$670
DUPONT (Dividends)	319	275
TROPICANA	88	81
TIME WARNER	-71	—
DUPONT (Unremitted profits)**	337	134

*Estimates

**After-tax earnings

DATA: COMPANY REPORTS, FIRST BOSTON, BZW CANADA

ways try to sell something to Seagram."

So far, diversification has worked best on the spirits side, where the addition of the new brands has been accompanied by a restructuring of Seagram's traditional portfolio. Convinced that as consumers drink less, they will trade up to better brands, Bronfman has refocused Seagram on premium brands such as Chivas Regal and Glenlivet scotch, and sold off low-end labels such as Lord Calvert whiskey and Wolfshmidt vodka. "They were long since past their peak," says Edward F. McDonnell, president of Seagram's Spirits & Wine Group.

The upscale shift appears to be working. Improved Asian distribution is now fueling double-digit growth at Martell, while Absolut should grow around 6% this year, to roughly \$300 million. The result: Liquor operating margins should top 15%, up from 12.6% in 1991.

By contrast, returns from Tropicana have so far been slim. Insiders say earnings—which have averaged well below \$100 million annually—have never come close to Seagram's expectations. Turn-

over has been heavy: As Bronfman sought to boost returns, Tropicana went through three presidents and a half-dozen marketing chiefs in the first five years of ownership. And this revolving door has been costly. After Tropicana in 1988 introduced Twister, a fruit-based drink, sales of the hot brand hit \$250 million in the first two years. But as management turmoil shook Tropicana, Twister lost momentum to New Age competitors such as Snapple Beverage Corp. Twister is now languishing in the booming segment.

Now, things may finally be looking up. In early 1993, Bronfman recruited Ellen R. Marram, a well-regarded marketer who was president of Nabisco Biscuit Co., to head Seagram's nonalcoholic beverage group. She has since intensified an aggressive global expansion and a series of new-product launches that show signs of squeezing better performance out of Tropicana. Tropicana has expanded into Canada, western Europe, and the Far East. In the U.S., it has introduced new juices such as Grovestand, an extra-pulp version of Tropicana's premium orange juice. Altogether, Marram says, new products will bring 21% of Tropicana's estimated \$1.4 billion sales this year. Still, the expansion is expensive. Analyst Nattel believes Tropicana's operating income will fall 14% for 1994, to \$88 million.

HOOKED ON HOLLYWOOD. But with profits expected to strengthen over the next several years, Marram says analysts have been too quick to argue that Seagram overpaid for Tropicana. "You have to look into the future to answer that question," she says. Other buys are also imminent. A top-of-the-line tequila is a likely target, and observers think Tropicana must soon catch up in New Age drinks. "They're looking at beverages that can be marketed under the Tropicana name as an alternative to Coca-Cola Co.'s Fruitopia," says Joel Weiner, an ex-Seagram exec.

Bronfman is also trying to make his disparate empire function more efficiently. He recently hired Boston Consulting Group to help cut costs and focus Seagram's long-term strategy. Bronfman has given few signs of where the strategic review will lead. But if the guests at his recent wedding are any indication, he's still in love with Hollywood. Divorced in 1991, Bronfman recently married Clarissa Alcock, scion of a wealthy Venezuelan oil family. The singers Ashford & Simpson performed at the Caracas wedding, and Hollywood potentates Barry Diller, Michael Douglas, and Michael Ovitz were guests. Douglas delivered a toast to Edgar and Clarissa that described their relationship "as an example to us all." So far, the same can't be said for Bronfman's ambitious diversification strategy.

By Laura Zinn in New York, with Julia Flynn in London

EDITED BY OTIS PORT

CAN SOFTWARE BE TAUGHT TO BE FAIR?

SO YOU THINK COMPUTER software is value-neutral? Not according to William A. Wallace, a Rensselaer Polytechnic Institute professor of decision sciences and author of the 1994 book *Ethics in Modeling*. Wallace says one major U.S. bank had to fix its loan-evaluation software after discovering that it tended to reject some applications by putting too much weight on old age.

Many users, says Wallace, are not aware that computer models are often subtly shaped by the ethical judgments and assumptions of the programmers who created the software. He and RPI colleague Deborah G. Johnson, a philosophy professor, hope to prepare training materials, including a video, to sensitize people to the hidden ethics of "expert systems." There are legal issues as well. Wallace says it's unclear who's liable if something goes wrong with a computer model—its creator or the user.

A ROBOSUIT FOR RESCUE WORKERS

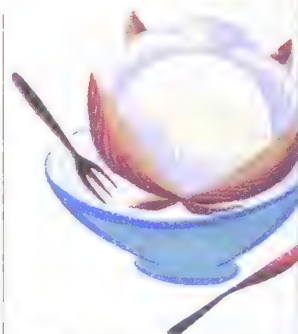
IF CALIFORNIANS ARE LUCKY, THE HUGE EARTHQUAKE that's due any day now will hold off a while longer—until an international team of researchers can finish developing a way to give rescue workers the strength of the Bionic Man. The idea is to combine a titanium suit of armor with robotics technology, especially at the elbows, knees, and other joints. There, battery-powered motors would provide five times the strength of human muscles.

Sensors and a built-in computer would track the wearer's movements and instantly cause the robosuit to mimic those movements. The technology is similar to that now used with virtual-reality gloves. But instead of just sticking your hand in a remote-control mechanism, you would climb completely inside the robot. After donning the robotic armor, tomorrow's knights could ride to

the rescue in the aftermath of a tornado, say, and help free people trapped under heavy debris.

Head tailor for the robosuit is Kazuo Yamafuji, a professor at the University of Electro-Communications in Tokyo. He hopes to have a prototype in two years, with help from Sergei Ulyanov of the Russian Academy of Sciences and Maria Feng, an assistant professor of civil engineering at the University of California at Irvine. They

plan to integrate robotics technology from several Japanese companies, Russia's space program, and the U.S. Defense Dept. Two Japanese construction companies, Takenaka Corp. and Shimizu Corp., are providing the initial funding.



HEY, LET'S CHOW DOWN ON SOME TASTY COTTON

A MOUTHFUL OF COTTON for real, not just an annoying morning-after sensation. That's the goal of Roghaye Narayan, chairman of the Chemical Engineering Dept. at Texas Tech University. With fabrics using increasing amounts of synthetic fiber, Narayan wants to help Texas farmers find new markets for their cotton crops by grinding cottonseed into flour or a coarse meal that fit for consumption by people as well as livestock.

Trouble is, cotton plants naturally produce a nasty pesticide called gossypol. While it's not a lethal chemical, it will make people and animals sick. So Narayan is perfecting a better and more cost-effective method for removing the gossypol, based on the technology used to decaffeinate coffee: so-called supercritical fluid extraction. Narayan has tailored the process to use propane and carbon dioxide for sucking the gossypol out of cottonseed. Why propane? Well, West Texas also has propane in abundance, so Narayan is killing two birds with one stone.

More important, Narayan says that using propane promises to be significantly cheaper than the current technique, which uses a hexane solvent. Because hexane is itself slightly toxic, meal made from cottonseed these days can be used only as livestock feed.

A SMALLER, BUT STILL SUPER, COLLIDER

FOLLOWING MONTHS OF financial haggling, the European Center for Particle Physics, better known as CERN, handed the world's physics community a welcome present last month: CERN's governing council voted to approve construction of a superconducting supercollider that will rival the power of the \$11 billion SSC killed by the U.S. Congress in 1993.

To hold down costs to \$2 billion, CERN's Large Hadron Collider (LHC) will be

only a third the size of the SSC's 57-mile-long ring. But thanks to stronger magnets, the LHC will be 80% as powerful—smashing subatomic particles together with enough force, CERN predicts, to untangle most enigmas surrounding the existence of matter. And the next generation of colliders may be considerably smaller and cheaper, yet more powerful. Chan J. Joshi, an electrical engineering professor at the University of California at Los

Angeles, is working on a laser technique that can accelerate particles to the necessary velocities 50 times faster than magnets can. Joshi says his laser accelerator won't be ready for 15 or 20 years.

Meantime, the LHC could be built in as little as 10 years. It'll take a bit longer if CERN's 19 member countries have to foot the whole bill. But there has already been talk in Washington of chipping in \$400 million of the cost to assure that U.S. scientists get in on the ground floor.

MEET THE FAIREST OF THE FAIRS

Where business is finding the best young minds

Frederic M. Niell III built his own cyclotron for basement experiments in particle physics. Richard Caldwell designed a new type of wing for planes. Sarita Maria used neural networks to develop a "smart" speech-recognition system so helicopter pilots could bark commands instead of flipping switches. And Kendra Bird discovered a fungus that may become a commercial source of taxol, a cancer-fighting agent.

Top researchers at America's high-tech companies? Not yet, anyway. You're teenagers, and these were your science fair projects.

It's no secret that precocious students have gone way beyond the mere experiments of a decade or two ago.

Westinghouse Science Talent Search awards 10 scholarships each year to seniors whose work regularly rivals graduate research for originality. In 1995, Niell, Caldwell, James, and Bird—respectively from Memphis, Tenn.; Corsicana, Tex.; Fort Wayne, Ind., and Blackfoot reservation near Brownsville, Mont.—weren't among the 40 Westinghouse finalists. They were participants in the International Science & Engineering Fair (ISEF), a global competition that dwarfs the Westinghouse prize. The last round of science fairs drew more than 1.5 million entrants, compared with only 1,645 for Westinghouse. Yet the ISEF is virtually unknown among U.S. business leaders.

Frederic S. McLaren is out to change

that. McLaren is president of Science Service Inc., a not-for-profit company founded in 1921 to promote science among students, including publishing *Science News*, a weekly magazine. Since taking the helm in 1991, McLaren has been trying to drum up more interest in the ISEF, now in its 46th year. But the former attack-sub skipper has found the going rough. "To my knowledge, no member of Congress has ever been to a fair, let alone a President or a Vice-President," McLaren says. Yet Westinghouse winners are regularly feted at the White House.

The recognition gap between the two competitions is all the more ironic because Science Service runs both of them. The Washington (D.C.) organization conceived the idea of the Science Talent Search in 1944 and has administered it ever since. Westinghouse Electric Corp. chips in \$500,000 to pay the bills and underwrite \$205,000 in scholarships. McLaren sees two reasons for its greater fame. First, Westinghouse does a masterful public-relations job. Second, the top Westinghouse prizes are \$40,000 scholarships; the fattest ISEF awards, until recently, were \$500.

McLaren is turning up the heat on company sponsors in hopes of increasing the prizes in all 16 science categories



CLASS ACT: Ford's project won him a spot at Intel

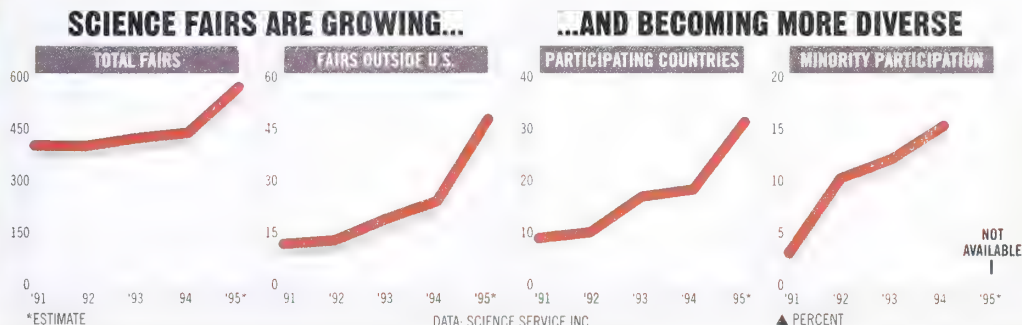
ries tenfold. With the help of pioneers such as Imax, Lockheed, and Phillips Petroleum, things are looking up. Intel Corp. has nearly quadrupled its support of the 1995 ISEF, to \$70,000. "It's important to get more kids involved early in science and technology," says Chairman Gordon E. Moore.

"ABSOLUTELY AMAZED." What really tipped the balance, though, was the report card turned in by Intel's Eugene S. Meieran, one of nine Intel scientists honored for their outstanding performance with the title of fellow. Meieran represented Intel at the past two science fairs and was "absolutely amazed" by the students' work.

In fact, one 1993 exhibit was so impressive that Meieran persuaded Intel to hire the student, Eric B. Ford, then 15, for a six-week summer internship. Now a junior at St. Andrews Episcopal School in Jackson, Miss., Ford



McLAREN: In search of science and funds



took second place in the Earth & Space category—plus six other awards from such sponsors as NASA and the Air Force. Total worth: \$1,050. They stemmed from reading about NASA's plan to send mobile robots to Mars and how vital it was to give the robots enough smarts to explore the treacherous Martian landscape. Ford decided to develop a navigation system using neural networks, and it became his ISEF entry.

"It was really fascinating—very advanced and technologically sound," Meieran recalls. So Intel brought Ford to California and put him to work with an engineering team that was developing a neural-network program for spotting causes of manufacturing defects in Intel's chips. Says Meieran: "Eric was a serious technical contributor to a program that involved very complicated and advanced technology."

McLaren wonders how many more budding scientists could be making contributions. "Why wait until these kids finish college?" he asks. "They're bursting with fresh new ideas now." Unfortunately, says Intel's Meieran, "most companies are much more interested in sponsoring a Little League team than in sponsoring a science fair."

The 1995 ISEF will be held on May 7-13 in Hamilton, Ont., featuring 1,200 projects—the best from 560 science fairs in the U.S. and 30 foreign countries. Some may also be honored in future Westinghouse contests, since roughly 85% of all Westinghouse winners cut their teeth at a science fair.

FUTURE STARS. Other participants will no doubt be tomorrow's entrepreneurs and scientists. The fairs that Hartley D. Peavey entered in the 1950s were the foundation of Peavey Electronics Corp., a Meridian (Miss.) manufacturer of sound equipment for rock musicians. Although he once yearned to be a rock star, Peavey's success in local fairs helped him realize he was better at building guitars than playing them. He started the business after he graduated from college in 1965, and today privately owned Peavey Electronics has 27 factories and 2,200 employees—and hundreds of millions in revenues. "Without the science fairs," Peavey wonders, "who knows where I'd be?"

Then there's Dr. Jud W. Gurney, an associate professor of radiology at the University of Nebraska Medical Center. He entered his first science fair in 1970, as a sophomore. While he got only as far as the state contest, he earned a four-year scholarship to the University of Nebraska. That helped convince his mother that science was a viable career. She had hoped he'd become a musician.

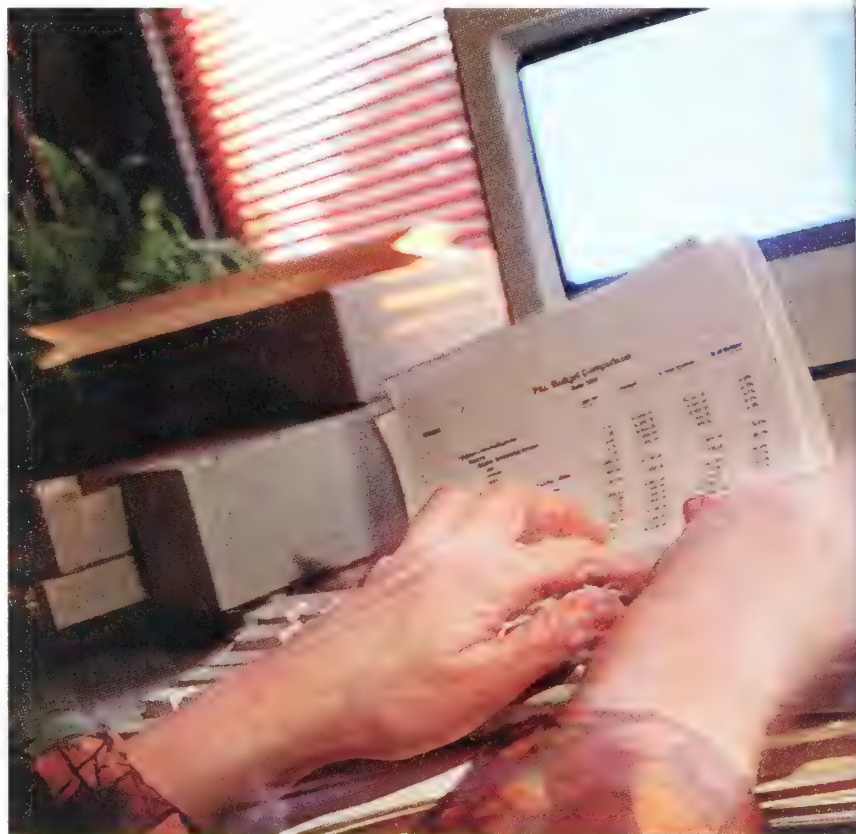
By Oles Port, with Ruth Corcoran, in New York

Legal Affairs

REPETITIVE STRESS INJURIES

THE ASBESTOS CASE OF THE 1990s?

Keyboard makers face a reckoning with injured workers



Nancy Urbanski first noticed pains in her hands in 1991. A secretary and registrar at a high school in Eagan, Minn., she spent many hours each day typing. And she was using her keyboard even more than usual to help launch a new record-keeping system at the school. By the time she sought medical care, Urbanski's affliction, repetitive stress injury (RSI), had caused her permanent damage.

Urbanski, a 30-year-old mother of two, isn't alone. She is one of thousands of similarly afflicted workers who aren't just looking to their employers for satisfaction. They're going after the keyboard makers themselves. In at least 25 states, plaintiffs are suing virtually every keyboard maker for selling flawed products and for not warning them

WRISTS AT RISK: Reported cases of RSI are up 770% from 10 years ago

about their potential risks. The scope of the litigation, dubbed the first white collar mass tort, is so vast that it could become the nightmare for Corporate America in the 1990s that asbestos was in the 1980s. "There's a gargantuan universe of victims," argues Urbanski's lawyer, Steven J. Phillips.

Keyboard makers ensnared in the legal morass include such blue chips as AT&T, IBM, Digital Equipment, and Eastman Kodak. Although the keyboard makers all deny wrongdoing, plaintiffs say manufacturers deliberately concealed the health risks associated with keyboard use—a charge that, if jurors accept, could trigger multimillion-dollar

ve awards in addition to compensa-
ones. "Average American workers
t have a clue about the potential
er," says Phillips, who made a mint
suing asbestos manufacturers.
ufacturers had an obligation to give
a clue."

H TITANS. On Jan. 3, the most for-
le offensive yet against manufac-
s was launched when Urbanski's
against first-time defendants IBM
Apple Computer Inc. opened in
eapolis. Phillips' firm, Levy Phillips
nigsberg, has spent years winning
ns of dollars from asbestos manu-
ers and other businesses. With its
ial clout and bevy of lawyers, the

motion, are up an astonishing 770% from
10 years ago (chart). Symptoms range
from minor aches to disabilities so se-
vere that some sufferers can't hold a
knife and fork. "This is by far the No. 1
injury we've had to deal with, ever,"
says Audrey A. Browne, a union lawyer
representing 130,000 New York City
municipal employees.

Although RSIs primarily afflict blue-
collar workers, they are becoming more
commonplace—and costly—in offices.
Liberty Mutual Insurance Co., the na-
tion's largest workers' compensation in-
surance carrier, says wrist injuries alone
stemming from repetitive motions cost it
\$50 million in 1989, the most recent year
for which figures are avail-
able. *CTD News*, a Haverford
(Pa.) newsletter about cumu-
lative trauma disorders,
puts the annual workers'
compensation tab for all RSIs
at \$2 billion.

Now, with RSI lawsuits
mounting, business costs
could multiply exponentially.
But collecting millions from
corporate titans such as IBM
and Apple will be tough.
Keyboard makers insist they
still don't know what actual-
ly causes some workers to
suffer injuries while others
remain perfectly healthy.
Many doctors and scientists
contend that a host of fac-
tors can cause RSIs, including
an individual's medical condi-
tion, job satisfaction, hob-
bies, and the ergonomic set-
up of each person's
workstation. "There are peo-
ple who are being injured,"
says Robert F. Bettendorf,
president of the corporate-
sponsored Institute for Of-
fice Ergonomics in Manches-
ter Center, Vt. "But the link
to the keyboard or anything else has
not been made."

Without conclusive scientific proof,
manufacturers say it would be impos-
sible for them to craft meaningful warn-
ings for customers or to design so-called
safer keyboards. In court papers, IBM
calls the plaintiff's charges "ridiculous."
IBM states: "Plaintiffs are attempting to
place the cart before the horse.... They
attempt to have a court of law resolve
what the science community has not
been able to do." Both IBM and Apple
decline comment on pending litigation.

In the few suits to make it to court
already, inadequate scientific proof has
tripped up plaintiffs. Last year, a Texas
jury sided with Compaq Computer
Corp. when it found that plaintiffs failed
to show a link between keyboards and
injuries. And an Arizona judge threw
out another suit brought by U S West
Inc. employees for insufficient evidence.

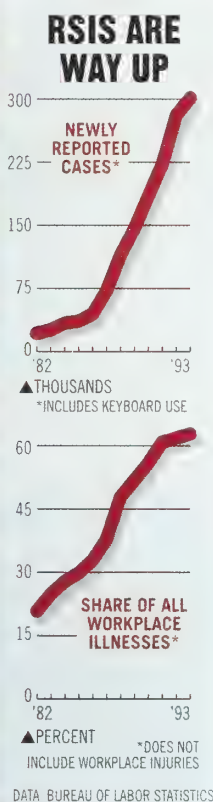
Phillips says the Urbanski case is dif-
ferent. IBM, for example, has repeatedly
stated that its keyboards are safe. But,
according to court records, IBM's expla-
nation for numerous occupational inju-
ries to its own employees, filed as part
of workers' compensation claims, is ex-
tensive keyboard use. From 1987 to
1991, IBM reported a fourfold increase in
the number of RSI claims made at 24
of its locations, court records show, as
well as a fivefold hike in costs incurred
from cumulative trauma disorders. IBM
states in court papers that the increase
is a reflection of its campaign to better
document employee problems, not "a
willful disregard for individual welfare."

LIKE TENNIS. As for Apple, plaintiffs
plan to show jurors an 11-minute video
produced internally in 1991 that fea-
tures several doctors and engineers dis-
cussing RSIs related to the keyboard.
In the video, keyboard workers are ad-
vised to take breaks from typing and
pay attention to pains as they occur.
Plaintiffs wonder why Apple would
make the video if it believed its product
was so benign.

Victor E. Schwartz, a product-liability
defense lawyer, says the plaintiffs' argu-
ments will ultimately fail. He believes
jurors will blame keyboard users for
not exercising common sense. "It's just
like when you use a tennis racket over
and over again," explains Schwartz.
"People know to take a break."

Win or lose, the RSI litigation and
surrounding controversy have already
had some impact. The government is
developing mandatory ergonomic stan-
dards due out later this year. Microsoft
Corp. and Compaq have recently begun
putting warning labels on their key-
boards while several companies are sell-
ing alternative keyboards they claim
are safer than older models. "The com-
puter industry, at least its lawyers, rec-
ognizes it needs to take measures to
protect itself," says Keith R. Mestrich,
an occupational safety and health spe-
cialist for the AFL-CIO. The question for
workers and companies alike is whether
that recognition has come too late.

By Linda Himmelstein in New York



has put together a case against
and Apple filled with scientific ex-
and previously undisclosed com-
records. The Urbanski trial could
defining event: A loss will diminish
iffs' hopes for mega-verdicts, while
tory could open the floodgates to
ss litigation.

employers and companies alike are
ning the trial closely—particularly
RSIs have become the fastest-
ing workplace illness in the U.S.
which are muscular or skeletal dis-
s caused by the strain of repetitive

As a key case comes to trial, thousands of lawsuits are
pending against virtually every keyboard manufacturer

COMPUTERS

IT JUST MAY BE THE YEAR OF THE APPLE

It's leaner, it's signing up clone makers—and the Intel and Windows woes won't hurt a bit

Will 1995 be Apple Computer Inc.'s year? A lot could go wrong between now and next December, but the once-beleaguered computer maker is starting out with the brightest prospects in years. Taking a more liberal approach to licensing its technology, Apple has just signed the first two Macintosh clone makers and is negotiating with nearly a dozen more. It's positioned to cash in on the boom in home and school markets. And fate has been kind: A technical snafu in Intel Corp.'s Pentium chip gives buyers a new reason to consider Power Macs, which use the speedy (and so far flawless) PowerPC chip. Even better: Microsoft Corp.'s Windows 95 operating system—regarded by industry watchers as a potential “Mac Killer”—has been delayed.

Apple's new year began early with the Dec. 28 announcement of the first clone: A Silicon Valley startup called Power Computing Corp. Then, on Jan. 4, Radius Inc. a maker of Macintosh displays and software, disclosed plans for high-end Mac clones. More deals could soon follow. Insiders at Apple say the company is knee-deep in talks with Toshiba and Olivetti. And discussions are progressing with Motorola, Hitachi, Goldstar, Zenith Electronics, and German PC giant Vobis Microcomputer. FirePower Systems, a startup backed by Japan's Canon, is also eyeing the MacClone business, and consumer-electronics giant Pioneer could be making Mac compatibles by mid-1995, say sources close to Apple.

BOOSTER SHOT. Apple officials aren't confirming anything beyond Radius and Power Computing. But, says Don Strickland, Apple's vice-president for licensing: “The good news is we have licensees signed, sealed, and delivered.”

How good? The known Mac-maybes represent nearly 7% of the global PC market. That, in itself, could greatly aid Apple's goal of doubling the market share for Mac and Mac-compatibles, to 20%, in five years. Mac clones would not only bring in licensing fees but would broaden the Mac base, giving software

developers greater incentive to create Mac applications. Also, more Mac-compatible computers will mean more sales of highly profitable Apple peripherals such as laser printers.

But there are risks, too. The biggest is that the cloners will overwhelm Apple the way PC cloners swamped IBM in 1980s—undercutting its pricing and stealing market share. Also Apple is notorious for laying out ambitious plans, then failing to execute. If the clone strategy doesn't work, Apple has almost no chance of hitting its 20% market-share goal. Instead, it would languish in a market increasingly dominated by Microsoft Windows. So Wall Street remains leery: Of 25 top analysts, only five have a buy

on the stock, which now trades at around 39—far from its high in the 60s. “This is impressive. Is Apple moving in the right direction? Yes, unambiguously so,” says analyst William M. Bluestein of Forrester Research Inc. “Should it have been done sooner? Yes, unambiguously so.”

To be sure, Apple has had a rough-and-tumble journey in the 18 months since the board replaced Chief Executive John Sculley with Chief Operating Officer Michael H. Spindler. After suffering its largest quarterly loss and shedding 16% of its workers, Apple turned itself into a

lean fighting machine. For the quarter ended Sept. 30, revenues hit a record \$2.5 billion, up 16% over 1993. Profits were \$114.7 million—strong but shy of the pre-turmoil era. Eugene Glazer of Dean Witter Reynolds Inc., who recently went bullish on Apple, expects sales to jump 19%, to \$10.9 billion, and profits to rise 53%, to \$475 million. Glazer says Apple's stock should hit 50 by year-end.

The picture could grow brighter if the Wintel camp (comprising PC makers using Microsoft Windows and Intel chips) loses momentum. So far, buyers are still snapping up Wintel machines. And at Apple's Cupertino (Calif.) headquarters, the official stand is to take the high ground. Says Spindler: “It happens



LICENSING CHIEF STRICKLAND: A million Macintosh clones by '97

best." But privately, workers are ang and hoping to capitalize on Win- es. Says David C. Nagel, general ger of AppleSoft, the division that ps Apple operating systems: "Any a competitor makes a boneheaded one can only applaud that."

h mistakes could produce more ntum for the Power Macs. Intro- last March, Power Macs are sell- o well that analysts now say the any will ship 1.2 million units the ear, 20% above Apple's target. For two, Apple has a bunch of new PC-based machines, starting in or June with a PowerBook laptop. Second-generation Macs are due by 1995. Now in development under a of colorful code names—TNT, Tsu- and Nitro—some use the most ful PowerPC chip yet, the new 604. **RNAUT.** The new year will also a Newton revival plan. The much- ned handheld communicator got a on Jan. 4 with the introduction of ola Inc.'s Marco, a \$900 to \$1,400 al communicator that uses Newton ology and actually does what Apple ised two years ago: send and re- all types of electronic messages ssly. On Jan. 30, Apple is set to its updated Newton, code-named e, to be followed midyear by e," a software update with im- d handwriting recognition.

THINKING MAC

EXISTING LICENSEES

Power Computing, Radius

MAC MAYBES

ASIA Fujitsu, Toshiba, Goldstar, Hitachi, Pioneer

EUROPE Olivetti, Vobis

NORTH AMERICA FirePower Systems, Motorola, Zenith Data Systems

DATA BUSINESS WEEK

Apple has a turnaround plan for eWorld, its online service, too. So far, it has only 55,000 subscribers. In mid-1995, the Mac-only system will be offered to Windows users and—more important—Apple plans to spin it off into a separate company, perhaps as early as this month. That would bring a big capital infusion, most likely from a Baby Bell. Apple is in talks with U S West Inc., according to sources close to the PC maker.

Despite all the plans, Apple could find itself back on the defensive before the year is out. The delay of Windows 95 gives Apple a breather, but the new operating system is still a huge threat.

Software testers say it finally gives Windows Mac-like ease. Even if it does not appear until late 1995, it will be on the market well ahead of "Copland," the Mac operating system update slated for mid-1996. Copland has such advances as software "agents" that automatically perform tasks. But by the time customers see this stuff, the Windows juggernaut may have done its damage.

That makes Apple's bid to license the Mac technology even more critical. Its plan calls for licensees to sell over 1 million Mac compatibles by 1997. That would give the Mac camp approximately 3 more percentage points of mar-

ket share. Pieter Hartsook, a Mac market analyst, predicts 500,000 Mac clones for 1995 and 1.6 million in 1996.

Power Computing alone says it can sell 100,000 Mac clones this year—all by mail order. That would sound nuts for a startup if not for President Stephen Kahng. He's the engineer behind the Leading Edge Model D, a mid-1980s PC clone that helped pioneer the mass-market PC business. Besides selling Mac clones under its own brand, Power Computing will build clones for other PC makers to sell. One likely candidate: Olivetti, its largest outside investor.

But, analysts say, Apple still needs a deal with an industry megaplayer, such as IBM or Compaq. A Mac clone from IBM could "bust the market wide open," says analyst Richard J. Zwetchkenbaum of International Data Corp. IBM, which has toyed with licensing the Mac software for the common PowerPC hardware design the two companies agreed to in November, would be ideal. But Big Blue is unlikely to jump soon: The Windows 95 delay gives IBM a fresh shot at making inroads with its OS/2 operating system in the coming months. Laments one Apple insider: "We need at least one major company and one strong in business."

Meanwhile, the clone game begins. Kahng vows to be "very competitive with Intel machines." That could mean Mac compatibles retailing for \$1,000—vs. \$1,800 for the cheapest Power Mac now. Apple execs aren't losing sleep, though. They concede there could be a "little" market-share erosion, but they expect clone makers to expand the market and Apple's slice with it. Besides, they say, they've learned how to cut prices and stay profitable. With 27% gross margins, they're ready to go toe-to-toe with the likes of Compaq and Dell. Says Nagel: "We're in much better shape today than we've been in, well, forever." That's why 1995 may truly be Apple's year.

By Kathy Rebello in Cupertino, Calif., with bureau reports



Apple may need a deal with a biggie such as Compaq or IBM. A clone from IBM could "bust the market wide open," says one analyst

COMPUTERS

HOW TOSHIBA'S LAPTOPS RETOOK THE HEIGHTS

Vibrant screens and cool-running chips helped win the day

It didn't take much for Toshiba Corp. to lose its title as the world's leading maker of laptop computers. By taking its eye off the ball for a single personal-computer product cycle—about a year in human terms—the Japanese giant squandered the lead in a market where it once boasted a 40% market share. It was a lot harder to retake the lead. But with surprising speed, Toshiba reversed its slide and is now on top again. This time, can it stay?

Maybe—if the company's executives don't forget the lessons of the past few years. After launching the T1000 line, the first successful IBM-compatible laptops, in 1985, Toshiba consolidated its lead by continually cutting prices and adding features. But in the early 1990s—just as the competition was heating up—it began to skimp on research, misgauged the market with bulkier machines when rivals were shrinking their models, and, worst of all, failed to incorporate the latest microprocessors as quickly as the competition. A host of new entrants charged ahead, and by 1993, Toshiba had fallen to No. 2, behind Compaq Computer Corp.

CUT LOOSE. Now, Toshiba has regained its balance with fleet-footed marketing by a more independent U.S. operation and a big investment in engineering. In 1994, according to International Data Corp., Toshiba grabbed 15.6% of the worldwide portable computer market, compared with Compaq's 14% (table). In the critical U.S. market, Toshiba did even better, capturing 17.8% vs. Compaq's 14.7%.

How did Toshiba pull it off? By beating Compaq—and others—to market with cutting-edge and aggressively priced models. In the last few months, Toshiba slashed prices on some models by up to \$1,200. "It used to take six months to a year for a new [generation of computers] to go from desktop to laptop," says Atsutoshi Nishida, president of Toshiba America Information Systems Inc. in Irvine, Calif. "But from 1993 on, we've introduced a notebook product on the same day that Intel introduces a new chip." Toshiba's Performance T4900CT note-

book, introduced last October, was the first laptop using the P54C, a low-power version of Intel's Pentium. By devising "heat pipes" to cool the hot-running chip, Toshiba's engineers built the machine without an internal fan—saving precious battery power. The less exotic T4800CT, meanwhile, has gotten rave reviews for its vibrant color display and five-plus hours of battery life.

The management change that made all this possible was Tokyo's decision to give the U.S. subsidiary more say. "There was a

TOSHIBA'S T4900CT:
Aggressive pricing and better research

time when Tokyo took the initiative on product development," says Tetsuya Mizoguchi, head of PCs for Toshiba in Japan. "We have grown up since then."

And Toshiba's U.S. marketers have made some astute calls on what the market wanted, and when. "They are using leading-edge technology but not way out there on the bleeding edge," says Mark MacGuire, an analyst with market researcher Dataquest Inc. For example, when IBM and Compaq added inexpensive subnotebook PCs, Toshiba introduced

the fully featured color Portégé—and avoided a market gaffe. Customers for the cheaper subnotebooks were underpowered, and both IBM and Compaq had to drastically cut prices.

Toshiba also got lucky. Its fiercest rival, Compaq, has become the No. 1 maker in the world. But it has let its notebook line slip. Its Conturas, for example, lacks some of the power management and multimedia features of rival products. "Recently, Compaq has been making a lot of mistakes," says Nishida. There have been problems, concedes Laurie L. Strong, Compaq's vice-president for portables and software. "We concentrated on other things," she says. "Certainly, Toshiba is our No. 1 competitor, but I'd put us neck and neck." Strong says Compaq is patching up any holes in its lineup. Still, Toshiba has some advantages Compaq can't easily match, including the fruits of its huge investment in screen technology. Rebuilding Windows would make color screens de rigueur.

Toshiba and Intel plowed \$250 million in a joint venture, Display Technologies, to build thin-film transistor, or TFT, color displays. In August, they announced plans to spend \$400 million to double capacity at its **RED CAPE**. The screen edge may soon end. The No. 1 maker, Sharp Corp., plans to hike production in 1995, a Mitsubishi Electric Corp. said on Dec. 27 that it will break ground in March for a \$400 million TFT plant. So Toshiba is focusing on other technology: lithium-ion batteries and multimedia gadgets such as built-in CD-ROM drives.

By retaking the lead, Toshiba is again the competition's prime target. Gateway 2000, a perennial wannabe in notebooks, has high hopes. The mail-order PC maker says its Liberty laptop, with a 10.4-in. display and high-capacity (up to 700 megabytes) disk drive, will undercut Toshiba's pricier Portégé. Says Alberto G. Giazzone, director of marketing: "The portable market is very product-oriented. It allows you to jump up in market share quickly, but it means you have to defend it constantly." Just ask Toshiba.

By Larry Holyoke in Tokyo
with bureau reports



Back on Top

Estimated 1994 shipments worldwide of notebook and laptop PCs

1994 RANK	COMPANY	UNITS SHIPPED THOUSANDS	MARKET SHARE	1993 RANK
1	TOSHIBA	1,217	15.6%	2
2	COMPAQ	1,093	14.01	1
3	IBM	771	9.88	5
4	NEC	700	8.97	4
5	APPLE	655	8.4	3

DATA: INTERNATIONAL DATA CORP.



**COMMUNICATIONS, HARDWARE, SOFTWARE, AND MANAGEMENT
CORPORATE IT STRATEGIES FOR THE NEXT STAGE**

**Summary of the Business Week Information Revolution Conference held
October 31-November 1, 1994 at the McGraw-Hill headquarters in New York**

This stuff is really going to change our entire civilization," says **Dr. Michael Nelson, Special Assistant to the President for Information Technology.** This "stuff" is

digital tidal wave of 1s and 0s that is revolutionizing the way information is stored, retrieved, created, and moved. Digital information technologies will be as important as the printing press and as important as the invention of electricity itself," he added.

Nelson and other presenters from more than 150 chief information officers at Business Week's Information Revolution conference in New York City met to discuss how to harness the power of the digital technology that is shaping business and society worldwide.

The Information Revolution has been building steadily. Over the

last 30 years, computing power per chip has doubled every year and a half. At the same time, advances in fiber-optic transmission technologies have vastly increased the capacity of the telecommunications network to interconnect those chips. And now, the development of new digital wireless technologies is further augmenting the usefulness of computer services through greater mobility—connection from anywhere, to anywhere, at any time.

But revolutions sometimes devour their children. And as the world gets caught up in a digital fury, realizing IT's promise of improved efficiency, creativity, and profitability will demand IT that is both sound and prescient.

WANTED: CRYSTAL BALL

Sound IT management is something close to clairvoyance. Being simultaneously future-focused and level-

headed is essential for IT managers who want a good return on their investment. **AT&T Network Systems Atlantic and Canadian Region President Carleton Fiorina** says CIOs can make it easier on themselves if they avoid two common mistakes that diminish the potential of their investments.

"First, keep in mind that IT is a long-term proposition," says Fiorina. "Don't focus on first costs as opposed to life-cycle costs. As a corporation, you are making huge bets when you invest in a particular technology today—on its flexibility, its capability to evolve over time, whether it will serve customer needs, and whether it will do so cost effectively."

Second, Fiorina says "Don't lose sight of the customer. Companies must ask themselves, 'What is the experience end-users are looking for and how can this technology help us provide that end-user experience?'"

"Too often decision makers become seduced by technology, shifting their focus from the customer to technology for technology's sake—a dead end. If technology can create the right experience for the end-user, can create value for which an end-user is willing to spend money with you rather than with anyone else, then that's the right technology; if it can't, then it's the wrong technology, no matter how sophisticated it is."

WHO'S IN THE DRIVER'S SEAT?

These issues bring up a fundamental question posed by the IT revolution—does technology drive business change? Or do business needs drive technology? "They drive each other," says **Aetna Life and Casualty Chairman, President, and CEO Ron Compton**, "and competition drives them both."

Compton says the rapid changes that characterize IT have put unprecedented pressure on business to meet escalating customer expectations. But he cautions that, in their eagerness for technology to enhance competitiveness, companies remember that IT is a tool that, if used wisely, enables businesses to perform essential processes faster, better, and cheaper.

"Technology alone does not a revolution make. Business needs and consumer needs trump technology every time." At Aetna, Compton has outlined an IT policy that may seem simple, but provides an essential framework for every IT decision the company makes. "We use IT to optimize our business processes so we can deliver products and services to the customers in the most effective, efficient way—and to do that better than the competition."

FROM POTS TO PANS

The Information Revolution is not about technology in search of a problem. AT&T's Fiorina says, "Customers have problems, and they are looking for solutions." With the rapid advancement of IT, customer expectations have never been higher, and there is mounting pressure for immediate, inexpensive, high-quality solutions to their needs.

It is that pressure that has propelled AT&T Network Systems to the fore of developing the "information infrastructure" required to meet the growing demands made of technology. So AT&T is moving from POTS, "plain old telephone service," to PANS, "pretty amazing new stuff" to meet customer needs.

AT&T is one of the companies most actively deploying the new information infrastructure technologies that will facilitate interactive broadband services for businesses and consumers.

The Clinton Administration is working with companies like AT&T as it constructs a national information infrastructure (NII), Nelson notes. The NII will be a system providing all Americans the information they want, when they want it, where they want it, at an affordable price. "The NII will involve many builders, many technologies. We're excited. We think the global infrastructure, of which the NII is ultimately a part, will change every aspect of society and the economy."

A RETURN TO TERMINALS?

Roel Pieper, President and CEO, UB Networks, says that's not the half of IT. He sees the present inter-con-

nectivity of information and people through networks like the information superhighway and the Internet as catalysts for fundamental change in business networking—change that should be taken lightly.

Pieper suggests that as IT changes business to make processes more efficient and to push decision-making to the customer, the present PC-on-desk model may not adequately address the problems of keeping that information current and secured.

"I would challenge the model that is represented today by the PC. We need another model where the device that actually presents that information access point is not a PC, but is more like a terminal. And that the actual PC becomes more like a work-group server." Pieper envisions client-client/server, or client-server/server models, models in which data is staged from a mainframe to the business process work-group no further, and then from the business work-group to intelligent or dumb terminals. "Yes, it is a re-centralization, only to a degree—just far enough to get the information more effectively into the business process," says Pieper.

Safeguarding the integrity of information vital to competitiveness is a concern shared by **Oracle New Product Marketing Vice-President Cullen**. Cullen says that while the scope of corporate information has evolved beyond text, methods for man-



CATHERINE S. FIORINA, PRESIDENT, ATLANTIC AND CANADIAN REGIONS, AT&T NETWORK SYSTEMS

"If technology can create the right experience for the end-user, can create value for which an end user is willing to spend money with you rather than with anyone else, then that's the right technology."



ROEL PIEPER, PRESIDENT AND CEO, UB NETWORKS

"I would challenge the model that is represented today by the PC. We need another model where the device that actually presents that information access point is not a PC, but is more like a terminal. And that the actual PC becomes more like a work-group server."

new information forms have not. "Information is corporate critical for wise decision-making while we know exactly what our assets are because we manage structured databases," says Cullen. "We have had no idea what our real assets are because we have no management capability for our e-mails, memos, or videos."

Until now. Oracle's Media Server is the first multi-media data base for companies to store, manage, and retrieve all their information—text video, images, and even real-time feeds. Media Server acts as the foundation for application services and electronic agents that can help users within large corporations share and access multimedia document data. "Large companies supporting thousands of users and millions of documents can now have groupware capabilities built on a robust, scalable architecture," says Cullen.

TRANSFORMS PERSONAL COMMUNICATION

The management of personal communication is an equally important part of the new information age. In a recent innovation, Sony introduced its Magic Link Personal Communicator. Sony Magic Link enables mobile professionals to use intelligent messaging and personal information management capabilities. Sony has taken an important step forward

to improve the way people communicate," says **Carl Yankowski, president and COO of Sony Electronics,**

Using software technologies from General Magic and AT&T Personal Link Services, the portable device, slightly more than a pound, features integrated communications and organizing capabilities. Sony Magic Link allows users to send and receive e-mail from anywhere, organize meetings, manage daily tasks and appointments, send faxes, take notes, make phone calls, file, access the Internet and America Online, get stock quotes, etc.

"The first people to use Magic Link have significant communications needs and are already optimistic that this technology can maximize their productivity," says Yankowski. "We'll incorporate feedback from these initial users to grow the market for personal communicator products in coming years."

MAINFRAMES REDUX

The fast appreciation of corporate IT systems has catapulted the chief information officer to the top rungs of the corporate ladder. That's ironic. Not long ago the CIO was losing control over the organization's information thanks to the wild proliferation of PCs throughout the corporate and business units.

But **Charles Francis, vice-president, Information Technology Management and Financial Strategies, Comdisco** observes, "American businesses that could not abandon mainframes and distribute their control of technology fast enough just a few years ago, are now in the process of re-centralizing the control and management of their high-technology assets to their IS departments."

Francis says that the high-tech-in-every-office shopping spree that lavished \$500 billion on distributed products is over. Many businesses have become painfully aware that they cannot manage what they created. "They simply do not have the understanding, breadth of view, manpower, or expertise to make effective use of distributed technologies."

Enter the CIO, poised to regain control of the critical decisions and activities that relate information technology to business process reengineering. In this new environment, **Ernst & Young Center for Business Innovation Director Bernard Mathaisel** says that CIOs are called upon to play four distinct roles: technologist, utility manager, R&D director, and infrastructure builder.

"Our research reveals seven major processes by which a successful CIO applies leadership skills and resources to achieve information technology capabilities consonant with the needs of the business: communication of goals; engagement of resources; technology decision-making; provision for 'reality checks'; acquisition of new knowledge; assurance of rigor and honesty; and measurement of progress and results."

But above all, Mathaisel stresses the CIO's importance as a *disintermediator*—one ultimately responsible for multiplying the points of information access throughout the organization. The most important element in this pursuit is the creation of an enabling infrastructure.

"Think of the CIO as chief infrastructure officer," says Mathaisel. "Organizations want a solid foundation of basics, the delivery of some routine systems, the establishment of a backbone. World class operations at the



KITTY CULLEN, VICE-PRESIDENT, NEW MEDIA PRODUCT MARKETING, ORACLE CORPORATION

"Large companies supporting thousands of users and millions of documents can now have groupware capabilities built on a robust, scalable architecture."



CARL YANKOWSKI, PRESIDENT AND COO OF SONY ELECTRONICS

"Sony has taken an important step forward to improve the way people communicate."

basics level is a fundamental premise of CIO leadership; without it there will be nothing more than a squishy foundation, on which very little can be built."

Mathaisal says that from there, CIOs can go on to enable departments to fulfill their objectives, can take part in IT-enabled business process reengineering, and can play a greater role in formulating technology-enabled strategies and opportunities for the business.

But Mathaisal says it is difficult to remain focused on the enabling infrastructure that lies at the core of IT support for business change—it has no sizzle. People have no interest in it and the CEO doesn't want to talk about it. "The responsibility for an enabling infrastructure falls on the CIO," says Mathaisal, "as the only individual who can master the plan, build it creatively, and maintain it effectively."

NO MORE DENIAL

Whether CIOs decide to re-centralize or to extend distributed client/server solutions, they must do so at minimum cost. Not only must CEOs and CIOs worry about changing paradigms in information technology within the corporation, they must also worry about cost. The cost of client/server computing has become a key issue in large enterprises—though it's one many executives would rather ignore.

"People are under the impression that a wholesale migration to the client/server computing model will reduce total IT costs," says **Gartner Group IT Management Research Director Ken Dec**. Dec says that while many early client/server implementa-

tions have improved business processes, MIS managers are right to think that client/server will bring higher total cost when applied pervasively to mission-critical applications across the enterprise. The question is whether the higher cost is worth it.

The client/server model is a major shift in corporate computing philosophy, distributing substantial computing power onto end-user desktops, often outside the control of the MIS organization. That means more than one-third of client/server costs will be outside the central MIS budget, hidden in end-user department expenses. "Over a five-year planning period, client/server will represent an investment of \$50,000–\$60,000 per desktop user," says Dec.

"The costs of distributed computing environment are deceptive, informal and spread out across the organization," says **Vanstar Corporation Chairman and CEO William Tauscher**. Tauscher says that because PCs entered the IT world haphazardly, they grew and evolved with numerous informal, costly services. "PCs snuck in the back door. They were treated like personal devices, and were often handled outside of IT when it came to ordering etc." As a result, the support structures that developed around PCs were informal. "Now that companies are networking all the PCs," says Tauscher, "they are finding huge organizational problems and system-process flow problems related to managing these networks."

To help corporations get a handle on end-user costs, Vanstar has created Scope, a comprehensive, two-step process-cost estimator. In the first step the company answers a series of

questions to quickly and credibly inform organizations about their total cost of computing and compare the to a database of over 100,000 users.

Then, a mapping process reviews current end-user processes and highlights areas for improvement. The blueprint provides a universal model of basic processes, established cost drivers and important process considerations. Cooperative mapping against the universal model then uncovers hidden infrastructure and inefficient processes. Together, the blueprints and mappings highlight areas for change.

"Information technology is getting more complicated every day," says Tauscher. "And while it's a lot harder for businesses to understand everything they need to know for using IT to remake their business, it's never been more important. If companies want to stay competitive, they've got to get a handle on their IT, figure out what's out there, what it's costing them, and how to put it to work to do it right."

Martin A. Keohan is a New York-based business writer.



BERNARD F. MATHAISEL, DIRECTOR, ERNST & YOUNG CENTER FOR BUSINESS INNOVATION

"The responsibility for enabling infrastructure falls on the CIO, as the only individual who can master the plan, build it creatively, and maintain it effectively."



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"Now that companies are networking all the PCs, they are finding huge organizational problems and system-process flow problems related to managing these networks."

MEET THE FASTEST FIVE-FOOTER IN THE NBA

Bullets President O'Malley knows how to draw a big crowd

Alan D. Archibald had had it. When the chairman and CEO of Black & Decker Corp. in Towson, Md., last spring that Washington Bullets season-ticket sales for 1994-95 would leap, he called Bullets President Susan O'Malley to say he was considering canceling the company's order. It wasn't Black & Decker would be getting more for its money. The team hadn't made the playoffs since 1988 and was headed for the cellar this year.

When O'Malley went to work, she called Archibald and begged him to stay on for one more season. A turnaround, she promised, was at hand. Archibald had heard all that before, but O'Malley just wore him down. "If it hadn't been for Susan," he says, "we wouldn't have hung in there."

BY PRIZES. For O'Malley, such intense nurturing of ticketholders, combined with savvy marketing, has had a payoff: soaring attendance. And she is confident her stats will only improve. In November, the skinflint Bullets shelled out millions to sign young basketball sensations Juwan Howard and Chris Webber. Bullets owner Abe Pollin followed through by announcing on Dec. 28 that he would finance a new 23,000-seat arena in downtown Washington. If the planned arena from the 18,750-seat USAir Arena in suburban Landover, Md., goes through, O'Malley may have a financial alley-oop: a team and a spanking new facility to play as draws.

The 33-year-old Bullets president fully looks the part of the highest-earning female sports exec who wasn't leashed by her post. She sometimes is mistaken for a basketball groupie when mingling with the team. "People never get to see a five-foot-tall woman walk and represent a basketball team," says O'Malley, a sailing buff who lives in Annapolis, Md.



O'MALLEY: Candid about her family connections

And they probably don't expect anyone this candid: O'Malley readily concedes that family connections helped her get where she is. After a three-year stint with a Maryland ad agency, she applied in 1986 for an advertising post with the Bullets. Pollin, the team's owner, who also controls the Washington Capitals hockey team and USAir Arena, is a close friend of O'Malley's father, Peter.

A Slam Dunk in The Seats

SEASON	WIN PERCENTAGE	AVERAGE ATTENDANCE	SELLOUTS
1988-89	0.488	9,814	1
1989-90	0.378	11,565	4
1990-91	0.366	11,880	10
1991-92	0.305	12,341	15
1992-93	0.268	13,641	20
1993-94	0.293	15,116	19
1994-95	0.269*	17,000*	25**

* AS OF JAN. 3, 1995

** PROJECTED SELLOUTS

DATA: WASHINGTON BULLETS

ter. Pollin and the senior O'Malley, who was president of the Caps in the 1970s, deny they knew Susan was applying for the job, but she harbors no illusions. "I got the job because my father was good friends with Abe Pollin," she says. "But I like to think I moved up the ladder because of my accomplishments."

They've been impressive. When O'Malley was tapped to run the franchise's business operations in 1989, the Bullets were struggling on and off the court. Former Bullets Kevin M. Grevey recalls that when he donated some team tickets to a charity golf tournament a few years ago, "people were joking they were booby prizes."

STOKING SELLOUTS. O'Malley moved quickly to shore up fan support. The result of her efforts: Renewals by season ticketholders have averaged 90% in the past five years, vs. 61% when she took over.

She also has stoked demand with shrewd marketing ploys. For years, laggard teams used giveaways and other promotions to boost attendance at games against other also-rans. But O'Malley decided that promoting games against high-profile teams could make them sellouts. As the Bullets racked up more sellouts, fans were encouraged to buy 10-packs—tickets for the most popular 10 games of the season—to avoid missing the big ones. The sellouts prompt others to spring for season tickets. Promoting already popular matchups "went against the grain in the NBA," says Detroit Pistons CEO Tom Wilson. "But it's been copied throughout the league."

According to NBA sources, the Bullets lost about \$4 million in the 1987-1988 season before O'Malley took over. This season, the team should earn about \$1.5 million on revenues of about \$33 million. In September, Pollin gave O'Malley responsibility for sponsorship and promotion for his entire sports organization.

For lasting success, however, O'Malley needs a winning team. That's why the Bullets signed rookie Howard to a \$41 million, 12-year contract. The team also inked a \$2.1 million, one-year pact with Webber, who won rookie-of-the-year honors as a Golden State Warrior last year. While the Bullets' record remains dismal—and a serious injury to Webber on Dec. 22 may delay the turnaround—the team is playing with unaccustomed flair. "They're a much more exciting team to watch now," says Black & Decker's Archibald. But until the Bullets really catch fire on the court, O'Malley will need to keep doing what she does so well: fanning the flames from the sidelines.

By Amy Barrett in Landover, Md.

EDITED BY AMY DUNKIN

BUYING STOCKS LIKE CLOCKWORK

If one of your New Year's resolutions is to invest cash that has been building up in your bank account, or if your goal is simply to begin saving regularly, there is an easy way to get started. At major mutual-fund families and brokerages, you can elect to sock away a certain amount at regular intervals, and the company will perform the transactions automatically. This disciplined style of investing has many advantages—some purely psychological and others you can count in dollars and cents.

In these uncertain markets, more investors are opting for "automatic" (or "systematic") investing plans. The Strong fund family reported a 25% increase in automatic transactions during 1994. But the programs are not widely advertised. "Small transactions tend not to be very prosperous for the money-management industry," says John Keefe, a consultant to the financial services industry in New York. But, for investors, they can provide a painless way to build up hundreds of thousands in their accounts.

The foundation of any such program is dollar-cost averaging—the idea that when you invest a set amount, say \$100 a month, you buy more shares when prices are low and fewer when prices are high. This cuts your average cost per share and allows you to profit from volatility in a stock market that historically trends up. "The poten-

tial reward is greater than people realize," says Stephen Savage, editor of *Value Line Mutual Fund Survey*.

When you follow this method, you don't have to lose sleep over market slides, knowing that your dollars are going further. You also don't have to worry about moving all your money in just before a crash. Plus, removing emotion from decision-making greatly improves chances that you will still plug money into the market when it's on the way down. Besides, it's

more convenient than mailing in checks every month.

For people who are just starting to save, the automatic plans have obvious merit. Companies will withdraw small amounts of money from your paycheck, bank account, or money-market fund and use it to buy fund shares. You may not even

really miss the extra cash.

Some fund companies waive their minimum initial investment requirements for systematic investors. Janus, T. Rowe Price, and Strong, to name a few, waive minimums of \$1,000 or more if you agree to invest at least \$50 up to twice a month or just once a quarter. At discount brokerage Charles Schwab, all funds

in One Source, a network of no-load funds sold for a transaction fee, have a \$10 minimum for automatic investors. You can cancel the program anytime, but if you haven't reached the minimum initial investment, you'll need to add more to the account or liquidate your holdings. These programs are an ideal method for making monetary gifts to children, and some fund companies have special college-savings programs set up this way.

But automatic investing also can be useful if you have a large sum to invest, particularly if you are newly liquid because you sold a business, gained life-insurance benefits, or received the proceeds of your 401(k) plan, says Martin Jaffe. He is chief operating officer at Wood, Struthers & Whitrop, the investment management subsidiary of Donaldson, Lufkin & Jenrette. Lump-sum holders tend to be ve-



INVESTING

Some Automatic Investing Strategies

IF YOUR NEW YEAR'S RESOLUTION IS TO START SAVING Have \$50 or more withdrawn from your checking account each month and invested in a mutual fund. Many fund companies have no minimum balance requirements for automatic investors.

IF YOU'RE AFRAID OF PLUNGING A LUMP SUM INTO THE STOCK AND BOND MARKETS ALL AT ONCE Place the cash in a money-market fund and have set amounts transferred into a series of funds each month over the course of a year.

IF YOU WANT TO EASE INTO EQUITIES Have the interest from your bond or money-market funds automatically swept into stock funds. Or buy a series of bonds with consecutive maturity dates (a bond "ladder") and invest the coupons in stocks.

IF YOU FEEL YOUR PORTFOLIO IS OVERWEIGHTED IN ONE AREA Rather than sell all at once, set up a program to transfer a small sum each month from, say, a stock fund to a bond fund.



course of a year, according to a 1993 study by finance professors at Wright State University. But in years with declines, you would have done better to put it in gradually.

"After all," says WSU professor Richard Williams, "in most years, the market goes up."

Even people who have carefully structured investment portfolios may want to incorporate automatic investing. If you rushed out of bonds when rates started to rise, you may want to reenter the market gradually to take advantage of higher rates. You can do this either by transferring cash into bond funds or by gradually switching

from an equity fund into a bond fund. "We've been recommending dollar-cost averaging into the bond market for a while now," says Ian MacKinnon, Vanguard's head of fixed-income investing.

Most fund companies and brokerages also offer systematic withdrawal. By requesting that a certain amount be redeemed and sent to you in cash each month, retirees can turn equity holdings into regular income. Keep in mind, though, this forces you to do the reverse of dollar-cost averaging. To receive the same dollar amount, you will end up selling more shares when prices are low and fewer when prices are high.

You still should keep an eye on your fund when you invest automatically. While you don't need to monitor daily price changes, make sure the fund's performance is in line with its peer group and that no major changes in management have been made. But don't halt the program if the market starts to slide. As long as you stick with it, automatic investing can be a great way to impose investment discipline in the new year. *Amey Stone*

DON'T SHORTCHANGE LONG-TERM BONDS

Less than two-tenths of a point separates the yield on two-year Treasury notes

from the 7.9% of 30-year bonds. So why stick your neck out and go long when you can get almost the same return on a short-term note with a lot less risk? That's why many investors are choosing short durations. But the case for locking

some of your money in bonds of five years or more is growing stronger.

This hinges largely on the belief that the inflation threat is over. The Federal Reserve is likely to raise rates at least once more, but many economists believe the aggressive tightening of the past year will start slowing the economy in early 1995. That should keep a lid on in-

flation and interest rates. And for long bonds, that's good news.

to rise without investors taking a bath—if they confine investments to midrange maturities. Rates for 10-year bonds would have to hit 9.14% in a year for you to merely break even on the price when selling bonds bought at current rates, says Robert Rodriguez, president of FPA New Income Fund.

The shape of the yield curve is indicating that rates aren't likely to rise that high,

many bond analysts say. When the curve is steep—as it was in October, 1993, with 30-year T-bonds paying 6%, vs. 3% for short-term bills—that's an indication rates may rise. When the curve is flat, as it is now, or inverted—meaning that long-term bonds are paying the same or less than short-termers—that's often a signal rates will fall. Another way to

SMART MONEY

The Lure of Long Bonds

►The economy should start slowing in the first half of 1995, keeping inflation in check and causing interest rates to level off or drop

►With inflation at 3% and yields close to 8%, a 5% real return puts bonds at the high end of their historical range

►An 8% yield on Treasuries is close to the 10% historical average return on stocks, which are usually riskier

think of it is to draw an arrow at the long end of the yield curve, says Randall Merk, senior vice-president of portfolio management for Benham Mutual. "That's where the market thinks rates will go."

ZEROS' POPULARITY. Most people ignore this signal and chase the highest-yielding bonds. For example, now that short rates are rising, short-term bonds look good. But a flattening yield curve means those tempting returns aren't likely to last and

Bonds yielding nearly 8% offer returns almost 5 points above the current 3% inflation rate. Even if inflation hits a heady 4.5%, you still have at least a three-point margin of safety. "The current spread above inflation is at the high end of the range for real return," says Dennis Bushe, a fixed-income strategist at Prudential Securities. There's even some room for market rates

you have a large lump sum to invest, your returns will be better most years if you plunged it into the market right away rather than spreading it in over the

may leave investors having to reinvest at lower rates when these bonds mature. "What appears to be the least attractive option, that's what you should be doing," says FPA's Rodriguez.

Another plug for long bonds comes from comparing them with equities, which return 10% a year on average over the long term. With 8% Treasuries, you're getting awfully close to that return without the risk, as long as you have enough time to hold the bonds to maturity. Zero-coupon bonds look even better. Since they don't pay out interest until they mature, there's no risk you'll have to reinvest at lower rates if you hold them to maturity. Indeed, says Benham's Merk, money has been pouring into his zero funds for about two months. Because of their extreme price volatility, zeros are paying slightly higher yields than long bonds (15-year zeros yield some 0.16 of a point more than 30-year Treasuries).

COLLEGE GOAL. If last year's rout makes you skittish about long-term bonds, there are ways to hedge your bets. Stick with government bonds that, unlike municipals or corporates, have no credit risk. Choose maturities that coincide with a future goal, such as paying for college tuition or retirement. Or ladder your portfolio with bonds of different durations so that you always have some bonds maturing to reinvest at current rates.

Another option is to dollar-cost-average by investing a little bit during each of the next few months so you won't miss out if rates rise further. Investors with a long time horizon should lock in bonds each time they break 8%, says Bill Fish, an analyst at Donaldson, Lufkin & Jenrette. Whatever type of investor you are, you can't go too wrong putting 10% of your portfolio in a safe long-term investment paying nearly 8%. *Pam Black*

A HIT OF OXYGEN FOR MAINSTREAM MEDICINE?

During a game against the Philadelphia Eagles early in the NFL season, Dallas

Cowboys center Mark Stepnoski sprained his ankle so badly he had to be carried from the field. Team doctors classified his injury as severe, and from the looks of the swelling, it was a good bet Stepnoski would be out for



MONSTER MENDER: Pro teams are great believers in hyperbaric chambers

weeks. But after a few rides in the Cowboys' "space capsule," Stepnoski walked without crutches in two days and was back to blocking by week's end.

What the Cowboys refer to as their "space capsule" is a hyperbaric oxygen (HBO) chamber. The 4½-ft.-by-7-ft. steel container offers a unique form of physical therapy by facilitating the flow of oxygen to injured areas. As HBO units become more prevalent, the therapy will move beyond professional athletes to weekend warriors. An HBO device compresses ambient air while patients breathe pure oxygen through a mask. The higher air pressure within the chamber accelerates oxygen dissolution in the bloodstream. Thus, healing oxygen reaches

torn muscles and broken bones at up to 15 times the normal rate. And because increased oxygen flow constricts blood vessels, swelling is kept to a minimum.

Although it's a new fad in the National Football League—the Cowboys, San Francisco 49ers, and New York Jets all acquired HBO units during 1994—HBO therapy has been around since the 1940s, when the Navy used it to treat divers with decompression sickness, or

injuries, such as sprain strains, and fractures, mostly anecdotal. Thus, most insurers don't cover its use for those conditions, even though case studies show recoveries can be twice as fast. A serious sprain may take three one-hour sessions, fracture at least nine, \$100 to \$200 per hour.

FUNDED RESEARCH. There are more than 300 HBO facilities across the U.S., mostly hospitals to treat serious conditions. But as more teams invest in units and report improved recovery times, rehab specialists predict HBO will become accepted a physical therapy as ultrasound. "We're waiting for insurance companies to realize the benefits," says Dr. Anthony DiBlanda, director of the Function Spine Rehabilitation Center in Haverhill, N.Y.

DiBlanda is developing a research protocol for treating back patients with HBO. Studies are also under way at Temple University in Philadelphia and the University of British Columbia. Paul Reihart, chairman of Vancouver-based Calipre Technologies, which markets HBO units, says Calipre plans to back more research "to convince insurers and industry that HBO will get workers back on the job faster, just like it gets players back in the game faster."

If the case is made, many more people will be riding in space capsules to heal their earthly injuries fast. *Kate Murphy*



the bends. Only within the past two decades, however, has there been enough research on HBO to support other medical applications. Clinical evidence now supports—and most insurance covers—its use to treat burns and bone infections with vascular complications.

Yet proof of HBO's efficacy in treating minor trauma in-

WORTH NOTING

■ **CHARITY CHECK.** To make sure most of your charitable contributions go to programs, not fund-raising or administrative costs, review the Council of Better Business Bureaus' *Annual Charity Index*. The 1995 edition profiles 207 charities and includes details on spending. It costs \$14.95 (plus sales tax in Virginia and New York). Send a check payable to CBBB to Charity Index, Council of Better Business Bureaus, Dept. 023, Washington, D.C. 20042-0023.

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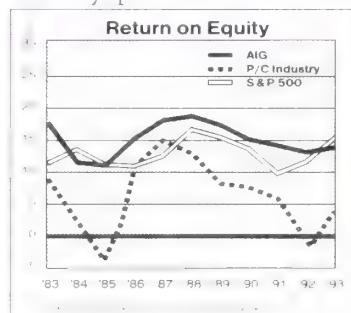
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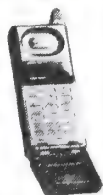
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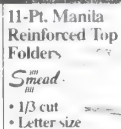
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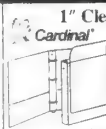
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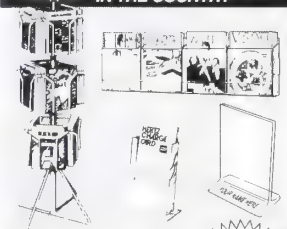
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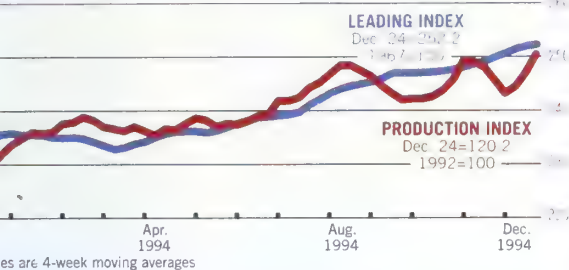
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Business Week Index

PRODUCTION AND LEADING INDEXES

Change from last week: 1.4%
Change from last year: 8.3%

Change from last week: 7.0%
Change from last year: 7.0%



Production index increased during the week ended Dec. 24, with gains in fully adjusted auto, truck, and steel output. Before calculation of the week moving average, the index increased to 123.2, from 121.5.

Leading index edged up only a bit in the latest week. Higher stock prices over business failures led the increase. The unaveraged index also fell a little, rising to 252.3 from a revised 252 in the week ended Dec. 17.

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BW Leading index copyright 1994 by CIBC

PRICING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
PRICES (12/30) S&P 500	460.94	458.82	-1.8
RATE BOND YIELD, Aaa (12/30)	8.43%	8.45%	21.5
INDUSTRIAL MATERIALS PRICES (12/30)	112.8	111.7	NA*
BUSINESS FAILURES (12/23)	267	331	-11.6
REAL ESTATE LOANS (12/21) billions	\$455.9	\$455.5r	8.7
CREDIT SUPPLY, M2 (12/19) billions	\$3,559.0	\$3,559.2r	0.8
UNEMPLOYMENT CLAIMS (12/17) thous.	325	323	-1.5

Sources: Center for International Business Cycle Research (CIBC), Standard & Moody's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures companies), Federal Reserve, Labor Dept. CIBC seasonally adjusts data on failures and real estate loans. *Historical data available from CIBC.

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
MUTUAL FUNDS (1/3)	5.98%	5.60%	3.03%
COMMERCIAL PAPER (1/3) 3-month	6.32	6.31	3.29
CERTIFICATES OF DEPOSIT (1/4) 3-month	6.38	6.37	3.25
FIXED RATE MORTGAGE (12/30) 30-year	9.18	9.34	7.24
ADJUSTABLE MORTGAGE (12/30) one-year	7.38	6.73	4.27
LIBOR (1/4)	8.50	8.50	6.00

Sources: Federal Reserve, HSH Associates, Reuters Holdings PLC

Data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

DEBT

Jan. 9 ▶ Consumers are expected to have added a hefty \$12 billion to their credit card debt in November, following a 1.6% increase of \$11.6 billion. That's the median forecast of economists surveyed by International, a unit of McGraw-Hill. The unit's forecast should account for a link of the increase. Both MasterCard International Inc. and Visa USA Inc. report a 1.6% increase in card activity vs. a 1.4% increase in November.

CONSUMER PRICE INDEX

Jan. 10, 8:30 a.m. ▶ The MMS

economists look for the December producer price index to rise by 0.2%, after November's 0.5% jump. The core index, which excludes the volatile energy and food sectors, is expected to increase 0.2% as well.

CONSUMER PRICE INDEX

Wednesday, Jan. 11, 8:30 a.m. ▶ The December consumer price index is expected to rise by 0.3%, says the median forecast, the same as in November. The core index should post a 0.3% increase as well. Price resistance by consumers is the chief reason why many producers cannot pass along their higher costs. Consumer inflation will end

1994 at about 2.7%, the third consecutive year that inflation has been below 3%.

RETAIL SALES

Friday, Jan. 13, 8:30 a.m. ▶ Retail sales in December are expected to have increased by 0.6%, following November's 1.2% gain. Excluding car sales, buying is projected to have been up by 0.5%. If the forecasters are right, real retail sales in the fourth quarter appear to have registered the strongest quarterly advance in eight years, and that includes the superstrong showings in the final quarters of both 1992 and 1993.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (12/31) thous. of net tons	2,045	1,995#	28.8
AUTOS (12/31) units	0	141,940	NM
TRUCKS (12/31) units	0	110,958	NM
ELECTRIC POWER (12/31) millions of kilowatt-hrs.	NA	59,421#	NA
CRUDE-OIL REFINING (12/31) thous. of bbl./day	NA	13,896#	NA
COAL (12/24) thous. of net tons	20,345#	20,504	28.8
PAPERBOARD (12/24) thous. of tons	NA#	NA	NA
PAPER (12/24) thous. of tons	NA#	NA	NA
LUMBER (12/24) millions of ft.	377.6#	499.7	12.2
RAIL FREIGHT (12/24) billions of ton-miles	23.7#	24.5	25.4

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA¹, SFPA², Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (1/4) \$/troy oz.	375.600	381.750	-5.0
STEEL SCRAP (1/3) #1 heavy, \$/ton	144.00	143.50	3.2
COPPER (12/31) ¢/lb.	142.4	140.4	66.2
ALUMINUM (12/31) ¢/lb.	94.0	91.0	77.4
COTTON (12/31) strict low middling 1-1/16 in., ¢/lb.	86.32	82.14	38.4
OIL (1/3) \$/bbl.	17.43	17.64	16.6

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (1/4)	101.21	100.32	112.30
GERMAN MARK (1/4)	1.56	1.57	1.74
BRITISH POUND (1/4)	1.56	1.54	1.48
FRENCH FRANC (1/4)	5.37	5.43	5.92
ITALIAN LIRA (1/4)	1626.5	1642.8	1694.5
CANADIAN DOLLAR (1/4)	1.41	1.40	1.32
MEXICAN PESO (1/4) ³	5.410	4.975	3.104

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

Fidelity Investment Challenge



LEADERS

Update #3 • Closing Values as of 12/28/94

Here are this week's leaders in the Fidelity Investment Challenge. On November 14, over 3,500 amateur investors began trading with a fictional 250,000 portfolio. Over the course of the next 3 months, they will buy, sell, or short sell any stock listed on the NYSE, AMEX, or OTC.

At the conclusion of the competition, February 10, 1995, the participant with the highest equity value will win a Eagle Vision TSi plus \$2,000 in cash. Other participants will win cash, Fidelity OnLine Xpress™ software and Market Master t-shirts for their performance.

THE TOP 30 AMATEUR INVESTORS

Rank	Investor	City, State	Equity Value
1	Jay Phisco	Cold Spring Harbor, NY	\$493,785
2	Jamie Weiss	Portsmouth, NH	\$430,126
3	William Miller	Murfreesboro, TN	\$399,355
4	Henry Sodke	Austin, TX	\$364,668
5	Charles Lechialo	West Newton, MA	\$362,985
6	Anatoly Raklyar	Brooklyn, NY	\$362,780
7	Eric Baird	New York, NY	\$350,780
8	Michael Wishner	New York, NY	\$347,453
9	David Evansen	Boca Raton, FL	\$345,724
10	Yizhak Peykar	Brooklyn, NY	\$344,633
11	Glenn Corbett	Arlington, VA	\$338,060
12	James Devine	Waldorf, MD	\$334,573
13	Mike Giffedder	Morristown, NJ	\$333,470
14	Peter Howard	Toluca Lake, CA	\$333,231
15	Robert Kratz	New Hyde Park, NY	\$331,859
16	George Mergenov	Longwood, FL	\$330,077
17	Ronald Cleveland	Memphis, TN	\$328,085
18	Dennis Hansen	Pittsburgh, PA	\$325,112
19	Marvin Miller	Sugarcreek, OH	\$324,787
20	Terry Hall	Burlington, MA	\$323,693
21	Robert Fisher	Chelmsford, MA	\$316,189
22	A. Robert Lawton	Wexford, PA	\$312,777
23	Jim Fox	Saginaw, MI	\$312,233
24	Mark Morgan	East Lansing, MI	\$311,726
25	David Bradley	Asheville, NC	\$311,725
26	Virgel Viets	Wethersfield, CT	\$311,331
27	Fenton Scruggs	Cleveland, TN	\$310,316
28	James Lugaresi	Glen Head, NY	\$309,130
29	Ramon Chen	San Anselmo, CA	\$309,122
30	Gregory Spencer	Sarasota, FL	\$308,931

THE COMPETITION UP CLOSE

Average Portfolio Value	\$243,336
Average Percentage Increase	-2.67%
Average Number of Trades Used	22
Portfolio Value of the 100th Ranked Account	\$285,283

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REPLICA

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Index to Companies

This index gives the starting page for a story or feature with a significant reference to a company. Most subsidiaries are indexed under their own names. Companies listed only in tables are not included.

A

Absolut 78
Advanced Micro Devices 60
Aetna 68
All American Gourmet 36
America Online 10
American Express 66
American Textile 42
Ames Department Stores 32
Apple Computer 36, 60, 84, 86
AT&T 38, 82

B

Bally's Grand 34
Banca Serfin 55
Bancomer 55
Bankers Trust New York 41
Baring Securities 42, 55
Bausch & Lomb 11
Bear Stearns 42
Beatrice 78
Benham Mutual 93
Bernstein Research 68
BevMark 6, 78
Black & Decker 91
Borland 16
Boston Co. 66
Boston Consulting Group 78
Bradlees 32
Brooklyn Brewery 6

C

Caesars Palace 34, 72
Calipre Technologies 94
Canon 84
Caremark International 38
CBS 38
Charles Schwab 92
Chrysler 42
Chubb 68
Cifra 42
Circus Circus 72
Citicorp 42
CNA Financial 68
Coca-Cola 38, 78
College Retirement Equities 78
Compaq Computer 60, 84, 86
Computer City 38
ConAgra 36
Continental 68
Corporación Industrial San Luis 42
Cyrix 60

D

Dataquest 86
Dean Foods 42
Dell Computer 84
Desert Inn 34

E

Detroit Pistons 91
Discount Tire 35
Display Technologies 86
Donaldson, Lufkin & Jenrette 92, 93
Dreyfus 66
DuPont 78

F

FirePower Systems 84
Forrester Research 84
FPA New Income Fund 93
Franklin Templeton 55
Fujitsu 84
F.W. Dodge 25

G

Gateway 2000 86
GE 35
General Foods 38
Global Information Solutions 38
Goldman Sachs 36
Goldstar 84
Goodyear Tire & Rubber 35
Grupo Carso 42
Guilford Mills 42

H

H.J. Heinz 36
Harris, Bretall, Sullivan & Smith 72
Healthy Choice 36
Hilton Hotels 72
Hitachi 84
HSC Software 16
Hyundai 15

I

IBM 38, 60, 82, 84, 86
Imax 81
Incredible Universe 38
Industrias Peñoles 55
Intel 16, 60, 81, 84
International Data 84, 86
Investors Group 78
ITT 34, 72
ITT Hartford 68

J

James Capel 55
Janus 92
J.C. Penney 32
Jenny Craig 36
J.P. Morgan 42
Johnan Shinkin Bank 6
J.W. Charles Securities 72

K

Kidder Peabody 78
Kmart 32
Kraft 36, 38

L

Leading Edge 84
Legent 38
Lehman Brothers 55, 76
Leifer Capital 70
Lipper Analytical Services 66
Lockheed 81
Loews 38
Lotus 16

M

Madison Square Garden 34
Marketdata Enterprises 36
Martell 78
Marvel Entertainment 72
MasterCard 99
McDonald's 28
McGraw-Hill 10, 25, 99
MCI 38
Mellon Bank 66
Mendocino Brewing 6
Merrill Lynch 70
Microsoft 16, 84
Mirage Resorts 34
Mitsubishi Electric 86
MMS International 99
MobileComm 16
Montgomery Securities 34, 42
Moors & Cabot 72
Morningstar 55
Motorola 16, 60
Multinational Strategies 42

N

Nabisco Biscuit 78
NBA 91
NCR 38
New Era Optical 11
New York Jets 94
NFL 94
Nomura Securities 76
Northern Telecom de México 42
NPD Group 37
Nutri/System 36
NYNEX/Olivetti 84
Oppenheimer 72
Organogenesis 72

P

PageNet 16
Pathfinder Research 60
Philip Morris 36, 38
Phillips Petroleum 81
Pioneer 84
Pittsburgh Pirates 31
Playtex Apparel 37
Polar 38
Portland Brewing 6
Power Computing 84
Procter & Gamble 60
Prudential Securities 93
Putnam Investment Management 42, 48

Q

QVC 38

R

Radio Shack 38
Radius 84
Regional Financial Associates 76
Revlon 72
Rich's Department Stores 32
R.R. Donnelley 42
Rubbermaid 35

S

San Francisco 49ers
Sara Lee 37
SAS 28
Schwartz's Intimate Apparel 37
Science Service 81
Seagram 78
Sears 32, 35, 37
Sequent Computer Systems 60
Sharp 86
Sheraton Hotels 34
Shimizu 80
Situr 55
SkyTel 16
Snapple Beverage 78
Spring Street Brewing
Standard & Poor's 68
Strong 92
Strong Funds 66
Sunkist 28
Synopsis 60

T

T. Rowe Price 92
Takenaka 80
Tandy 38
Target Stores 37
Tele-Communications
Teléfonos de México
Time Warner 6, 78
TLC Beatrice 4
Toshiba 84, 86
Transportación Marítima Mexicana 55
Tropicana 78
Twentieth Century Fund 11

U

U S West 84

V

Viacom 33
Vigoro 28
Visa 99
Vobis Microcomputer

W

Wal-Mart 32, 35, 42
Washington Bullets 9
Washington Capitals
Weight Watchers 36
Wells Fargo 4
Westinghouse 81
Wood Gundy 78

Z

Zenith Data Systems
Zurich Insurance 68

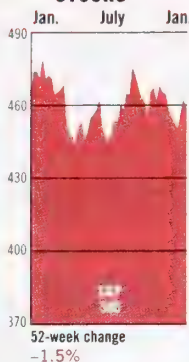
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Investment Figures of the Week

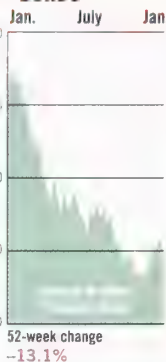
CURRENCY

acquaintance be forgot, tail sales and other re- economic strength carried mering inflation fears into Year. The yield on the 30- sury moved as high as Jan. 3, but a firming dol- ne prospect of another ate hike helped bring the eld down to 7.85% by Jan. ck market ended the an up note, gaining 19 outh of the border, Mexi- dent Ernesto Zedillo's y economic plan encoun- pticism.

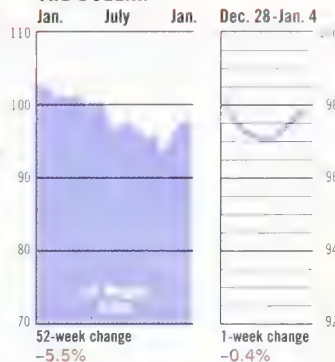
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS

	Latest	% change	
		Week	52-week
ES INDUSTRIALS	3857.7	0.5	1.5
COMPANIES (S&P MidCap Index)	169.0	0.4	-5.2
COMPANIES (Russell 2000)	247.7	1.0	-4.0
ANIES (Russell 3000)	263.8	0.2	-2.3
		% change (local currency)	
	Latest	Week	52-week
FINANCIAL TIMES 100)	3051.6	-1.4	-9.7
NIKKEI INDEX)	19,684.0	0.1	10.7
(TSE COMPOSITE)	4154.5	-1.1	-5.6

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.84%	5.59%	3.14%
30-YEAR TREASURY BOND YIELD	7.85%	7.83%	6.41%
S&P 500 DIVIDEND YIELD	2.81%	2.79%	2.48%
S&P 500 PRICE/EARNINGS RATIO	17.0	17.0	19.4

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 200-day moving average	457.6	457.8	Positive
Stocks above 200-day moving average	32.0%	30.0%	Positive
Speculative sentiment: Put/call ratio	0.61	0.59	Neutral
Insider sentiment: Vickers sell/buy ratio	1.06	1.07	Positive

BLOOMBERG FINANCIAL MARKETS

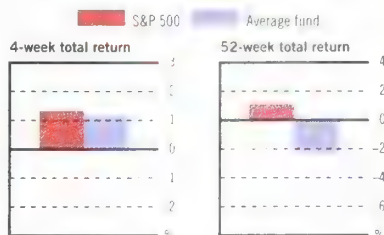
INDUSTRY GROUPS

INDUSTRY GROUPS	% change		Strongest stock in group	% change		Price
	4-week	52-week		4-week	52-week	
MINING	14.0	-7.2	CONSOLIDATED FREIGHTWAYS	17.5	-8.9	21 ⁷ / ₈
BUILDING	12.1	-42.0	PULTE	15.0	-35.2	23
OPERATES	8.4	-8.2	TELEDYNE	14.9	-20.6	20 ¹ / ₄
ING MATERIALS	8.3	-26.4	OWENS-CORNING FIBERGLAS	10.5	-27.7	31 ⁵ / ₈
ANCE BROKERS	7.8	-2.3	MARSH & McLENNAN	8.7	-2.2	79 ¹ / ₂
INDUSTRY GROUPS	% change		Weakest stock in group	% change		Price
	4-week	52-week		4-week	52-week	
ALTY APPAREL RETAILERS	-9.1	-17.0	THE LIMITED	-11.9	2.9	17 ⁵ / ₈
ND GAS DRILLING	-7.2	-19.9	ROWAN	-9.1	-29.6	6 ¹ / ₄
AL MERCHANDISE CHAINS	-6.2	-17.2	DAYTON HUDSON	-12.5	5.7	70
	-5.7	2.9	MATTEL	-7.3	22.0	25 ¹ / ₄
ALTY RETAILERS	-5.6	-5.8	TOYS 'R' US	-15.3	-23.8	30 ¹ / ₂

MORNINGSTAR INC.

MUTUAL FUNDS

S		LAGGARDS	
4-week total return	%	Four-week total return	%
ER WINTHROP REAL ESTATE INVMT.	11.2	WRIGHT EQUIFUND-MEXICO NATL. FID. EQTY.	-33.8
ONE AMERICA HARTWELL EMERG. GR. A	11.2	FIDELITY LATIN AMERICA	-19.8
REAL ESTATE SECURITIES	10.5	TCW/DW LATIN AMERICAN GROWTH	-19.2
52-week total return	%	52-week total return	%
MAN COMMUNICATIONS & INFORM. A	35.3	MONITREND GOLD	-50.2
JAPANESE SMALL COMPANY	29.5	STEADMAN AMERICAN INDUSTRY	-37.2
T SMALLER COMPANIES	28.7	STEADMAN OCEANOGRAPHIC TECHNOLOGY	-37.1



RELATIVE PORTFOLIOS

amounts represent the value of \$10,000 one year ago portfolio

ages indicate total returns

Foreign stocks
\$11,263
+0.14%

Money market fund
\$10,482
+0.31%

U.S. stocks
\$10,145
-0.16%

Gold
\$9,754
-0.30%

Treasury bonds
\$9,041
-2.03%

on this page are as of market close Wednesday, Jan. 4, 1995, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as

of market close Jan. 3. Mutual fund returns are as of Dec. 30, 1994. Relative portfolios are valued as of Jan. 3. A more detailed explanation of this page is available on request. r=revised

MEXICO STILL HAS A LOT GOING FOR IT

Wall Street to Mexican President Ernesto Zedillo Ponce de León: too little, too late. The Mexican stock, bond, and currency markets plunged following Zedillo's Jan. 3 speech outlining his emergency economic plan. An \$18 billion credit line. No wage hikes. Government spending cuts. Continued privatizations of state-owned assets. Yet the financial community is condemning the plan as insufficiently bold to stem the peso's collapse and restore investor confidence in the Mexican economy.

Give Zedillo a chance. Yes, his response to the peso's free fall was inept, and his much-delayed speech was less than stellar. Yes, there's still plenty of risk of social unrest and political turmoil in Mexico. But the substance of the plan has merit. Zedillo is strengthening the economic ties forged last year with the U.S. through the North American Free Trade Agreement, especially by opening up the banking system completely to foreign ownership. He's accelerating the privatization of the economy. And by getting the major labor groups to limit wage increases, he's offering some assurance that the inflationary impact from the devaluation won't set off a wage-and-price spiral. The Clinton Administration, without a peep of protest from the Republican leadership, reacted appropriately, pledging to lend support to the embattled Mexican government. So did private bankers and international financial officials.

In part, Wall Street's negative reaction to the Zedillo plan may reflect their past mistakes about Mexico. All last year, U.S. brokers enthusiastically flogged Mexican bond and stock holdings to individuals and to supposedly savvy institutional investors while playing down the risks of investing in developing countries. Besides, few money managers predicted a massive devaluation. This is reminiscent of the 1920s, when

Wall Street coined money by selling Mexican and other Latin American bonds to individuals—a strategy that backfired during widespread defaults in the 1930s. Back then, however, Mexico and other Latin American economies were dependent on highly volatile commodities.

Today, Mexico has a very strong industrial base and a growing middle class. A lot is going right in the real economy, and Zedillo, by speeding some key NAFTA reforms could end up strengthening the system even more. The problem lies more in the financial markets, where some key risks were glossed over and everyone tried to make too much money too fast.

The Mexican eruption is not the first financial crisis in the global spread of free-market economics. And it's not likely to be the last. A similar set of risks exists for almost every other developing nation, from Argentina to China, though not all will succumb. The developing nations are creating vibrant manufacturing and service economies by following the same free-market blueprint: bringing inflation rates down, reducing budget deficits, liberalizing trade, and privatizing publicly owned companies. Yet in coming years, all emerging economies will experience a difficult transition, Mexico has, from an authoritarian political framework to a more democratic system—a transition that will often create an economic or financial crisis.

The industrial world should do its best to keep instability in the developing nations to a minimum. But investors and industrial governments need to remember that in the emerging world, free-market capitalism is frontier capitalism. As anyone with a sense of American economic history should know, frontier capitalism is risky, but it pays off big in the long run.

TO CUT WELFARE, CUT THE NEED FOR IT

Like few other issues, welfare hits a nerve with Americans. With real wages still below their level of a decade ago, taxpayers have little desire to support the nonworking poor.

No wonder politicians are lining up to see who can be the most tough-minded. In their Contract With America, House Republicans vowed to deny benefits to unwed mothers under 18, with the savings being used for adoption, orphanages, or homes for unwed mothers. And to save money—\$40 billion over five years is the claim—House Speaker Newt Gingrich and his supporters would tighten eligibility, limit benefits to immigrants, and slash spending on food stamps and other programs by as much as 5%. Trying hard not to be outdone, President Bill Clinton is rethinking the welfare-reform plan he unveiled last June, which would have set a two-year limit on Aid to Families With Dependent Children and curbed benefits to new welfare mothers who refuse to establish paternity.

The current welfare system needs an overhaul. But as Clinton and the GOP get tough with welfare, something very impor-

tant is getting lost: the fate of the poorest children. The latest attempts at welfare reform are more likely to hurt children than help them. For example, denying welfare benefits to children without a legally recognized father would knock an estimated 2.8 million children off the rolls and into the streets, with disastrous long-term results. Similarly, curbs on food stamps may save money in the short run, but at the cost of more hungry and malnourished children.

That's why any attempt to fix welfare must focus on giving the children on welfare today the skills and health they need to be independent tomorrow. Educational-assistance programs such as Head Start should be strengthened. So should prenatal care. Perhaps families that take their children for regular health checkups, make sure their children attend school, and perform other acts that greatly improve their children's well-being should remain eligible for payments. A system structured to help welfare families focus on their kids is the best way to ensure that the welfare problem gets smaller, not larger.

BEHIND THE
SHAKEUP
BUSINESS WEEK
January 23

COMPUTERS PCs BY MAIL:
THE NEW BOOM

MARKETS THE MELTDOWN
IN LATIN AMERICA

BusinessWeek



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JANUARY 23, 1995

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DOWNSIZING

Corporate America did it.
Can Washington be
restructured,
too?

GOVERNMENT

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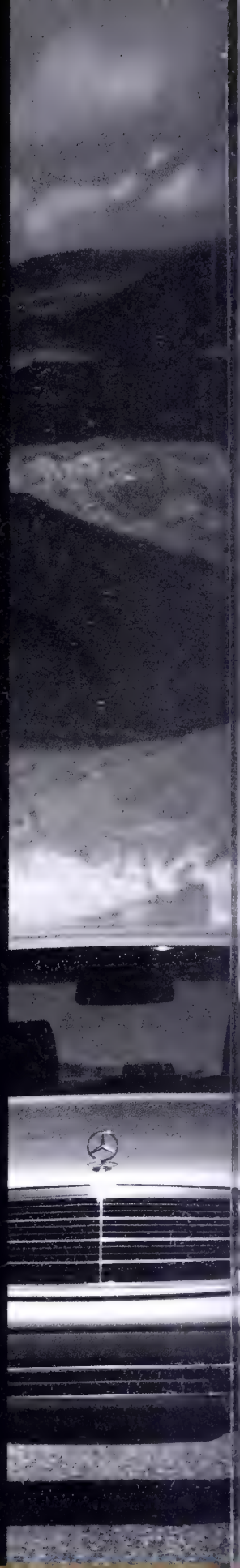
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YOU WOULDN'T BUY A CHEAP PACEMAKER.
YOU WOULDN'T BUY A CHEAP CRASH HELMET.
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Computer Systems



COVER STORY

SQUEEZE PLAY

Congress and Clinton agree that government should be smaller and more efficient—but just whose ox will get gored?

page 34



Cover Story

34 DOWNSIZING GOVERNMENT

Both Democrats and the GOP are racing to create a smaller, nimbler, more market-driven federal bureaucracy. But they could run smack into a major roadblock: Citizens clinging to their much-loved benefits

40 A TALK WITH VICE-PRESIDENT GORE

The Administration's point man on restructuring looks ahead

41 BUSINESS WEEK/HARRIS POLL

Is the public ready for less Uncle Sam and a greater role for the states?

News: Analysis & Commentary

44 THE APPLE OF ORACLE'S EYE

The database company covets the Mac as a weapon to best Bill Gates—and might launch a hostile takeover

44 FEED THE eWORLD

Apple is courting U.S. West to boost the prospects of its online service

45 CRYING FOUL ON THE FAIRWAY

The FTC may finally break the PGA Tour's lock on professional golfers

46 THE SAATCHI SLUGFEST, ROUND 2

The ad agency is rocked by mutiny, takeover talk, and a vengeful new rival: The ousted Maurice Saatchi himself

47 A SHOCKER AT GM

People like the electric Impact so much that the carmaker plans to make 7,500 of them in the next 18 months

48 SUSAN POWTER'S PAIN WITHOUT GAIN

A legal feud is costing the fitness maven a bundle. And it's not over yet

50 IN BUSINESS THIS WEEK

New FAA flight plan, Pillsbury, Mellon's Mr. Fixit, a Borland CEO, hockey's face-off ends, the Rubber Workers, J&J

International Business

54 LATIN AMERICA

The crisis in Mexico has spread to other markets, and investors will be sizing up plays with a much colder eye

58 MEXICO

The wreckage is much more severe than anyone imagined

59 A TALK WITH GUILLERMO ORTIZ

Mexico's Finance chief says "we have a short-term problem" but remains calm

60 JAPAN

A slew of top-level executives are studying the mysteries of *ki*

62 INTERNATIONAL OUTLOOK

Talking tough with Japan didn't work. Burying the hatchet won't either

Economic Analysis

26 ECONOMIC VIEWPOINT

Kuttner: Rewrite the regulatory rulebook—don't tear it up

30 ECONOMIC TRENDS

Dwindling population of the former Soviet Union, non-HMO docs, ex-welfare recipients, the cry for U.S. tax relief

31 BUSINESS OUTLOOK

If this keeps up, the Fed may come down too hard

78 COMMENTARY

Economists say welfare reform won't patch up poor families

Government

51 WASHINGTON OUTLOOK

The White House's new economic policy: Reelect Bill



MAKEUP AT BIG BLUE

Worried about prospects for its PC
business, IBM is reorganizing page 72



TAKE THAT

In the new cult of *ki*,
Japanese execs try to
harness the "life
force" in their
business careers

page 60



MOOS

Anyone
thought the
market
would be flat,"
said Waitt.
Gateway's
sales surged
50%



HIGH TECH ON THE HIGH SEAS

America's Cup '95: Forget about wooden ships
and iron men (or women) page 86

Science & Technology

DEVELOPMENTS TO WATCH

ed from feathers, in-flight video,
ter artificial blood, sharper maps
ARMAN BIOTECH BLOOMS—AGAIN
ading for startups is starting to flow,
looser regulations are in the works

Information Processing

TECHNOLOGY & YOU

e year to go nuts over Notes
GOOD NEWS ISN'T GOOD ENOUGH
reshuffling—despite healthy profits
o lessen its dependence on big iron
PC IS IN THE MAIL (REALLY)
ect marketing of computers takes off

Media

DO'S EXCELLENT ADVENTURE

ner's production companies are
roducing 39 feature films this year

Corporation

LIVING FIAT LIKE A FERRARI

olo Cantarella has the Italian
maker roaring again

83 COMEBACK AT CARBIDE

It has slimmed down—with a vengeance

Sports Business

86 THE AMERICA'S CUP

More than ever, this year's contenders
are marvels of high technology

87 THE BOC CHALLENGE

Round the world by grit, stars, and IBM

Legal Affairs

88 THE SWAT TEAM OF BIAS LITIGATION

Oakland's Saperstein law firm leads a
rush of employment-discrimination suits

89 "I SAW MY JOY CURVE FLATTENING"

Seligman helps fund bias plaintiffs

Finance

90 A BILLION-DOLLAR BET ON INDIA

George Soros picks a controversial
ex-McKinseyite to head his new fund

92 PERPETUAL-ACQUISITION MACHINE

Unheralded Dover shows that
conglomerates can still work

93 POWER PLAYS

Time to invest in electric utilities?

94 KEMPER: WHO WILL BUY?

CEO Mathis wants a quick sale

96 INSIDE WALL STREET

Drawing oomph from "muscle chips"
This biotech baby could catch cold
Amid the rubble, a Mexican gem

111 INVESTMENT FIGURES OF THE WEEK

The Workplace

101 DOCTORS WITH UNION CARDS

Private physicians are joining up
to do battle with big insurers

Personal Business

102 INVESTING: Emerging-market plays

FLYING: Tips for frequent fliers

SMART MONEY: Partnership protection

Features

6 UP FRONT

13 READERS REPORT

17 CORRECTIONS AND CLARIFICATIONS

18 BOOKS

Rothenberg: *Where the Suckers Moon*

109 BUSINESS WEEK INDEX

110 INDEX TO COMPANIES

112 EDITORIALS

Up Front

EDITED BY LARRY LIGHT WITH RUTH COXETER



PRIMARY PASHA: *The ex-gov*

AFTERLIVES

SUNUNU RISES AGAIN IN THE GOP

JOHN SUNUNU, THE EX-White House Chief of Staff, has been largely persona non grata within Republican circles since 1991, when he was forced out of the Bush Administration for allegedly abusing travel perks. But the 1996 race for the GOP Presidential nomination is getting under way, and winning the New Hampshire primary is essential. So the ex-governor of the Granite State is a hot political property again.

Thus far, Sununu's No. 1 candidate is Dan Quayle, if—as all signs indicate—the former Vice-President goes for it. After that, he says, “all

the Republicans are my second choice.” Among those seeking his help up north are Senator Phil Gramm of Texas and former Tennessee Governor Lamar Alexander.

But not Senate Majority Leader Bob Dole. Why? Sununu engineered George Bush's victory over the Kansas senator in the 1988 New Hampshire primary by convincing its taxophobic voters that Dole would raise their taxes. The irony is, in 1990, Bush—with Sununu at his side—agreed to do just that.

Meanwhile, Sununu has been keeping busy as a regular on CNN's *Crossfire*, hitting the lecture circuit, and—less visibly—as a business consultant. Example: He tried to convince the Philippine government to allow a stalled Westinghouse Electric nuclear power plant to go forward. Manila turned him down in December. *Owen Ullmann*

DIGITAL DEPUTIES

TRACKING DOWN THE SOFTWARE SWIPERS

BEWARE THE SOFTWARE COPS. Software publishers are intensifying a crackdown on piracy of their wares. The campaign is showing signs of success, says the Software Publishers

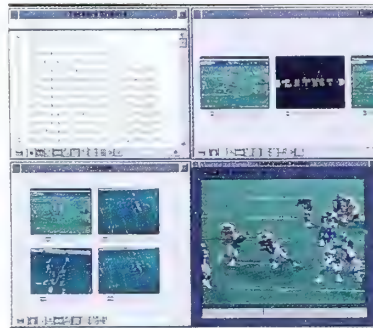
TALK SHOW “Virtuality at the mental level is something I think you'd find in most leadership over historical periods.”

—House Speaker Newt Gingrich, at conference on the Information Age, on how a leader must first form a vision before acting

SPORTS BIZ

SACKS, DRIVES, AND VIDEOTAPE

GAME FILMS HAVE LONG BEEN a key tool for football coaches to scope out the foe. Now, digital technology is speeding up the time-consuming chore of assembling the tapes.



COMPUTERIZED FILM: *Speedier*

The Chicago Bears, Cleveland Browns, and Green Bay Packers did their homework this season with the help of a digital tape-editing machine dubbed Sports Pro. The giz-

mo was developed by hot-growth company Avid Technology in Tewksbury, Mass. The machine whittles down the hours it takes to search through footage and cobble

various tape segments together. Third and two for the other guys? In minutes, the machine shows which plays next week's opponents are most likely to run.

The technology could not get the Bears, Browns, and Packers into their respective conference championship games, but look for wider use of it next season.

Avid is planning for the day when all game footage would be digitally stored in a central NFL library and customized tapes could easily be called up at any coach's workstation. *Carl Desens*

tion let them know that the practice is illegal. Plus, publishers are diligently suing over piracy, raking in \$14 million in judgments since 1988.

A top 1995 priority is the Internet, where hordes of small-timers are sending each other the latest filched goods. To combat that, the publishers now are fielding the “Infobahnmeister”—actually five undercover Internet flatfeet who will log on to bulletin boards and the Internet to monitor software exchanges.

There's also a cybernetic neighborhood watch forming—of bulletin-board managers. They're not joining out of civic-mindedness. They could get slapped with lawsuits if they don't root out pirates. □



REALITY CHECK

PRIVATIZING TELEKOM shows a commitment to reducing the role of the public sector in Germany's economy, says Chancellor Helmut Kohl's government. To Bonn, this is the only way for the state-owned telephone monopoly to go global. Set for sale to private in-

IN REALITY. Bonn is actually increasing its domination of Telekom as privatization nears. The government recently packed Telekom's new board with political appointees and civil servants. And look how Bonn just handled the award of the first license for a Germany-wide mobile-phone net-

vestors in 1996, Deutsche Telekom wants a global alliance with Sprint in the U.S. and France Telecom. But American regulators will approve such a deal only if they are convinced that Germany is really committed to opening its markets.



TELEKOM: *Globetrotter?*

work in airplanes. It chose DeTeMobil, a Telekom subsidiary. DeTeMobil aced out private-sector bidders Mannesmann Mobilfunk of Germany and Britain's Mercury Communications. So the question is: Will there be a level playing field in Europe's biggest market? *John Templeman*



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Up Front

NAME GAMES

EAST OF TRADEMARK EDEN

REBEL WITHOUT A CLAUSE—a consent clause, that is. The name of James Dean, the 1950s icon of brooding soulfulness, is used in Korea to sell fancy underwear, without the consent of his family. Result: a nasty U.S.-Korean trademark spat, the latest in a series of American complaints about alleged piracy of intellectual property in Asia.

Good People, a company founded by prominent Korean comedian and talk-show host Joo Byung-Jin, registered the late actor's name as a trademark in Korea in 1986. The upscale men's and women's undies, sold in "James Dean" shops all over South Korea, have done well, tripling sales between 1993 and 1994, to \$30 million. But



JAMES DEAN:
Boxer rebellion

in October, Dean's 90-year-old father and cousins, who own the marketing rights to the name, filed a trademark-infringement action in Korea. Only the Deans can approve use of the name, says family lawyer Mark Roesler, "and we want royalties."

Too bad. In November, the Korean Industrial Property Organization, Korea's overseer of trademarks, shocked U.S. officials by ruling that James Dean wasn't famous there, so no infringement occurred. U.S. complaints, though, have prompted the KIPO to review all trademarks to ensure proper consents were granted. Joo says he

may pay some royalties for Dean skivvies sold outside South Korea. Otherwise, he's unrepentant. He recently filed a \$1 million libel suit in Korea against Roesler, a suit that the Dean family's lawyer calls frivolous. *Douglas Harbrecht and Laxmi Nakarmi*

TECHNO CHIC

A CHIP ON YOUR SHOULDER—OR YOUR CUFFS

FORGET ABOUT INTEL INSIDE. Try Intel outside. The chipmaker is test-marketing a line of costume jewelry built from defective Pentiums. The test began in August, before the recent uproar over division errors in the Pentium chip,

INTEL OUTSIDE:
Sleek silicon

A multichip bracelet costs \$25, cuff links \$20—about 1% of the price of working chips.

No, it's not a clever way to dispose of buggy Pentiums returned by users in exchange for new chips. That stuff is melted down. The Pentium jewelry has defects that render them braindead on the production line.

Chipmakers have long used factory-reject chips in promo items such as key chains. About five years ago, ex-Intel staffer Dianne Emerson's Silicon Valley Ware first turned flawed 486 chips into jewelry for Intel people. Brisk demand prodded Intel to sell its next-generation rejects outside. *Otis Port*



but the notoriety helps. Stores at such high-tech centers as Stanford University have had trouble keeping stock. Chip jewelry is a bargain.

DRAWN & QUARTERED



I-WAY PATROL

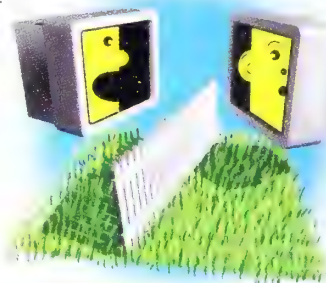
BYTE-SIZE BALONEY

ALLIGATORS IN THE SEWERS and other urban myths are longtime gossip staples. Now, the Internet is providing these myths with global distribution at warp speed. Few believed the fake wire-service report, recently circulating on the Net, that had Microsoft buying the Roman Catholic Church. But the old chestnuts making the rounds in cyberspace are harder to dismiss.

Consider the cookie-recipe revenge tale. A woman enjoyed some cookies at a café in a Neiman Marcus department store so much that she asked for the recipe. The waitress said there was a price for the recipe—"two-fifty"—and the customer charged it. When the bill came, the amount

was \$250. The irate customer was refused a refund. For revenge, she mailed out the recipe chain-letter style. No one knows who first put this story on the Net.

"This story has been circulating for years," sighs Liz Barrett, spokeswoman for Dallas-based Neiman. "We



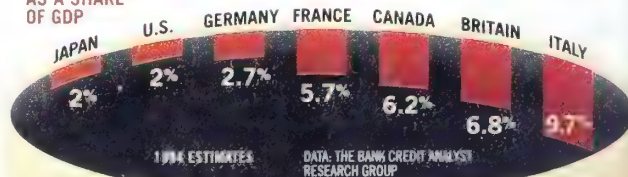
don't sell our recipes. We give them away, upon request." The store believes the cookie story evolved from a 1930s version that involved cake at New York's Waldorf-Astoria. *Julie Tilsner*

THE BIG PICTURE

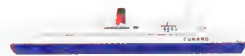
DEEPEST IN THE HOLE

BUDGET DEFICIT AS A SHARE OF GDP

Think the U.S. budget deficit is bad? Compare it to the other six major industrial powers'. As a percent of gross domestic product, only Japan does as well as America. One big reason: The others' greater social-service spending.



FOOTNOTES M. size or larger companies with managed-care health plans in 1991: 47%. In 1993: 58%. In 1994: 65%



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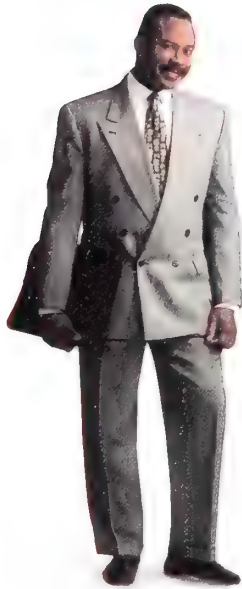
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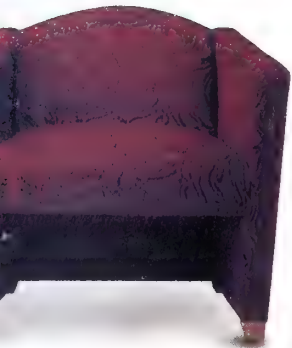
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INTEL'S PENTIUM: A STUDY IN FLAWED PUBLIC RELATIONS

Regarding your article "Bare knuckles at Big Blue" (News: Analysis & Commentary, Dec. 26), future generations of business school students will study Intel Corp.'s response to the problems with the Pentium chip as a classic case study in how to transform a technical problem into a public-relations nightmare.

Intel's five-point plan consisted of:

- 1) Initially deny that the problem exists;
- 2) When irrefutable evidence is presented that the problem exists, downplay its significance;
- 3) Agree to only replace items for people who can demonstrate extreme hardship;
- 4) Continue running your current ad campaign extolling the virtues of the product as if nothing has happened;
- 5) Count the short-term profits.

Leon Reinstein
Baltimore

THE WORLD WIDE WEB IS CHIC— BUT NOT YET DE RIGUEUR

Your In-Out list ("Hey, is that Sonny Bono driving a VW bug?" News: Analysis & Commentary, Dec. 26) claims that random Internet surfing is out and the World Wide Web is in. As a consultant specializing in the World Wide Web (www) and associated technologies, I can tell you that isn't happening...yet.

As proof, look at your advertisers. Excluding the special advertising section, there were 74 in your publication. Of these, two listed www addresses (Silicon Graphics Inc. and Intergraph Computer Systems) and one listed a private electronic bulletin board (Acre). That left 71 advertisers that had no reference to a www page, or even an Internet address.

In 15 minutes of Web-walking, I was able to determine that the following advertisers had a www presence: Apple Computer (www.apple.com), Compaq Computer (www.compaq.com), Hewlett-Packard (www.hp.com), Electronic Data

Systems (www.eds.com), Intel (www.intel.com), SAS Institute (www.sas.com), IBM (www.ibm.com), TRW (www.trw.com), AT&T (www.att.com), and, not to be left out, Microsoft (www.microsoft.com).

Until businesses start to advertise that they have a www address (noticeable by the prefix http://) and bring customers to them using the www as well as 800 numbers, the www will be a neat place to visit. But it won't be "What's In."

J. M. Ivler
Infobahn Xpress
Los Alamitos, Calif.

WHY SO MYOPIC ABOUT GLOBAL FREE TRADE?

In "Celebrate—and expand—free trade" (Editorials, Dec. 26), you properly extol the merits of negotiating a Western Hemisphere free-trade compact by the end of the 1990s. Why wait, you ask, for the officially set deadline of 2005?

Why, indeed. But, then, why wait till an even more distant date to implement a fully global free-trade strategy reaching out to as many countries as care to join us in such a noble endeavor? I have been urging this for 30 years.

You are not as farsighted as you ought to be. And you are insensitive to the need to protect legitimate labor interests at home and abroad and address environmental objectives as well. Neglect of these issues is a failing of virtually all the free-traders I know of.

David J. Steinberg
Alexandria, Va.

NO INTRIGUE, JUST GOOD RESEARCH

I would like to correct and clarify your article "Foreign intrigue in Jesse-land" (Up Front, Dec. 26).

North Carolina State University participates in USAID's Collaborative Research Support Programs (CRSPs) on peanuts, small ruminants, and soil management. A recent evaluation commis-

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earned a glittering REPUTATION as the GOLD STANDARD

of sedans.



With its SOPHISTICATED safety
systems, including DUAL AIR BAGS,

*New styling makes the Camry a
beautiful to look at as it is to drive.*





S GOLD.

POWER of an available V6 engine, and starting at only \$14,118,[†] Camry CONTINUES to make a NAME for itself.

The 1995 Toyota Camry. Newly RESTYLED. Yet with a HERITAGE of QUALITY craftsmanship that only the best REPUTATIONS are MADE OF.

Call 1-800-GO-TOYOTA for a BROCHURE and location of your nearest DEALER.



I Love What You Do For Me



Toyota Motor Manufacturing in Georgetown, Kentucky, which builds Camrys, received the Gold Plant Quality Award, North American Plant, two years running.

©1994 Toyota Motor Sales, U.S.A., Inc. Buckle Up! Drive for those who love you. *Camry LE V-6. Built in America. †Excludes tax, title, license, and serious injury, always wear your seatbelt. Driver and front-passenger air bags are a supplemental restraint only. ‡Manufacturer's suggested retail price w/o freight for DX 5-speed. Actual dealer price may vary. Camry LE V-6 shown with optional equipment. ††J.D. Power and Associates, 1994 and 1995 New Car and Light Truck Initial Quality Study. 1994 study based on a total of 14,016 consumer responses indicating owner-reported problems during the first 90 days of ownership. Most Camrys are built in America.

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Readers Report

DIRECTIONS & CLARIFICATIONS

caption on a photo with "Land mines on road to Utopia" (21st Century Capital-Bonus Issue, Nov. 18) should not have identified the armed men as Turkish soldiers. The women and children in the photo are Kurds lined up for food in the U.N. protection zone in Iraq. The armed men are not Kurds.

ed by USAID's Office of Agriculture and Food Security has confirmed that these have attained their objectives and benefited U.S. agriculture by producing crop varieties and technologies that resulted in economic benefits far in excess of the financial investments of USAID.

Continuation of these programs at current levels this year would result in a report of approximately \$4.5 million from North Carolina State University, of which nearly \$3 million would be transferred through sub-grants to Texas A&M University, the University of Hawaii, Cornell University, and the Agriculture Department. Consequently, North Carolina State University would receive net funds of approximately \$1.5 million, not \$3 million as reported.

Durward F. Bateman
Dean
College of Agriculture & Life Sciences
North Carolina State University
Raleigh, N.C.

Editor's note: The \$20 million mentioned in the story should have referred to the total amount of federal grants to North Carolina State, not just the agricultural programs.

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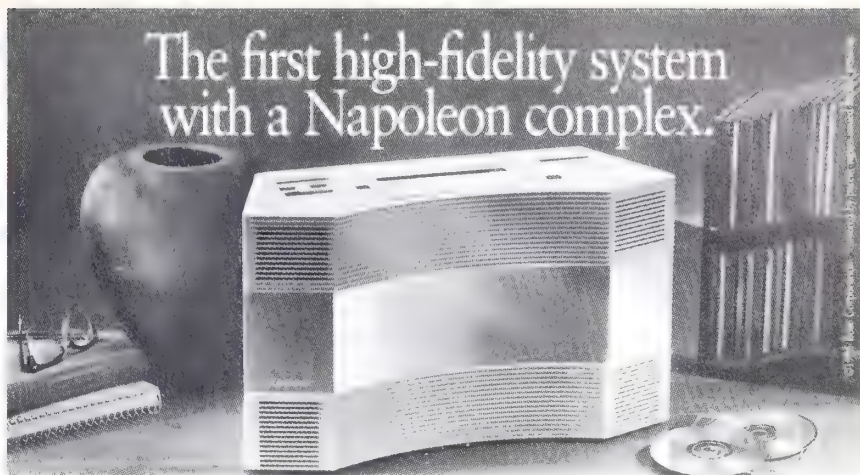
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HALFWAY THERE

A POWERFUL DRAMA FOR ALCOHOL AND DRUG ABUSE PREVENTION

Millions of teens use alcohol and drugs each year. *Halfway There* helps to change young people's perception about illegal alcohol and drug use.

Over 700,000 young people have experienced live performances of *Halfway There* in schools across the country and internationally.

For information about helping to make a difference by sponsoring *Halfway There* in your community contact:

periwinkle
NATIONAL THEATRE FOR YOUNG AUDIENCES

19 Clinton Avenue, Monticello, NY 12701 (914) 794-1666

This advertisement is a contribution to the national drug abuse prevention effort

WHERE THE SUCKERS MOON

An Advertising Story

By Randall Rothenberg

Knopf • 478pp • \$24.50

DRIVING BLIND ON MADISON AVENUE

Imagine the frustration of Subaru. In the late 1980s, your fellow Japanese carmakers seem to be on their way to taking over the U.S. auto market. But your market share remains infinitesimal. After 20 years, your durable little four-wheel-drive cars have won a following among the tofu-burgers-round-the-woodstove set, but that's about it.

What do you do? If you're Fuji Heavy Industries, the cars' manufacturer, and Subaru of America, their U.S. importer, you decide to reach for the big time with a new compact, the Legacy, which will compete with the likes of the Toyota Camry and Honda Accord. And you begin hunting for a marketing recipe and an ad agency that will transform your cars' image from reliable and quirky to luxurious and mainstream. "For image," as Randall Rothenberg writes, "of course, is destiny."

Rothenberg's *Where the Suckers Moon: An Advertising Story* recounts Subaru's effort to reinvent its image and secure a grander destiny. The author enjoyed extensive access to Subaru and the ad agencies that competed for its account, and he has emerged with an intricately detailed narrative of the process by which agency and client come together, collaborate—and come apart.

It's a woeful enough tale, told through the eyes of lots of flesh-and-blood characters. But there's a problem with the book that's inextricably linked to Subaru's frustration. Here are 426 pages (not counting notes) about a carmaker that commands some 1% of the U.S. market, and an agency, Weiden & Kennedy, that ranked 82nd among U.S.

agencies in 1993. In other words, Subaru's no IBM, and Weiden & Kennedy no Saatchi & Saatchi. Given the players' relative insignificance, the welter of detail here can be mind-numbing.

Still, one could ask for no better guide to Madison Avenue and the dynamics of the agency-client relationship than Rothenberg, a former advertising columnist for *The New York Times*. A skilled and skeptical observer, he has nicely captured the awful intellectual insecurity of the ad game. Ad agencies are constantly inventing diagrams, matrices, and quasi-academic studies to obscure the fact that most of what they do is based on intuition. They use this "pseudoscientific prattling," in Rothenberg's words, "to mask what are essentially well-founded opinions."

That's an example of what Rothenberg does best: plumb the motivations of his players and the structures of their organizations and industries, then use those insights to explain their actions. That lets him paint a rich and complex portrait of the competing agendas and hidden animosities that swirled around Subaru and its new agency, ultimately dooming both their relationship and Subaru's dreams of greater glory.

The conflicts began with Subaru of America's 1968 founding as an independent importer. While Fuji soon acquired 49.6% of the U.S. arm—and the rest in 1990—for most of their history the two companies had a weird, partly collaborative, partly competitive relationship. That hobbled their U.S. marketing effort, Rothenberg writes. "Subaru's ability to communicate a consistent message to the American public was contin-

ually confounded by Fuji's reticence sharing product-planning intelligence technical details, or pricing information until it was too late to incorporate the data into advertising and promotion campaigns."

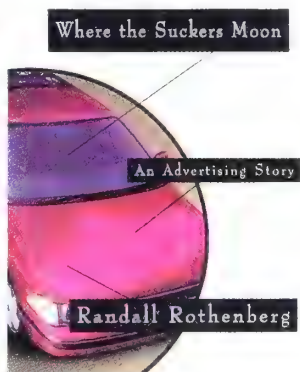
The hidden agendas really came into play once Subaru chose its new agency in 1991. Like many hot "creative" shops, Weiden, a Portland, Ore.-based firm famed for its ultrahip work for Nike Inc., essentially despised advertising. "In its television work... the agency considered itself a collection of filmmakers, not advertising types," Rothenberg writes. Its postmodern style was more an ironic, self-referential commentary on advertising and commercialism than an effort to sell its clients' products.

The result, for Subaru, was an artsy spot that mingled floating typography with factory images as a gruff voice drawled that "a car is just a car" and told consumers: "If it improves your standing with the neighbors, then you live among snobs with distorted values." Small wonder that the dealers—powerful constituency for any carmaker—were convinced Weiden cared only about winning ad-industry accolades, not selling Subarus. Relations between client and agency soured steadily. In 1993, Fuji installed a new head of Subaru of America who promptly renounced the mainstream strategy and fired Weiden.

Rothenberg's efforts to make up for the less-than-earthshaking nature of his material meet with varying success. At his best, he uses the particulars of his tale to illustrate broader issues in marketing, advertising, and the car business. Unfortunately, he's not content to leave it at that. Instead—much like Weiden & Kennedy with its ad—h wants his book to be a profound commentary on culture, history, and art. Along the way, he tosses out reference to everyone from Heraclitus to Bishop George Berkeley, adds in hermeneutic and semiotics, and tells us that Subaru's search for a new image was "central to America's understanding of itself as the 20th century dragged to close." It's too bad. Save for such overreaching—and 100 or so pages of minutiae—this is a vivid tale, acutely observed and smartly interpreted.

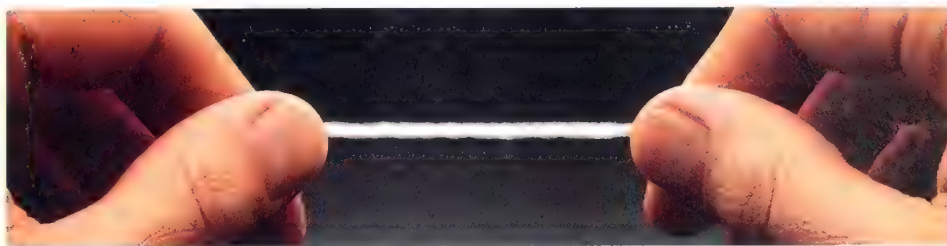
BY MARK N. VAMOS

Senior Editor Vamos covered the advertising industry in the early 1980s.

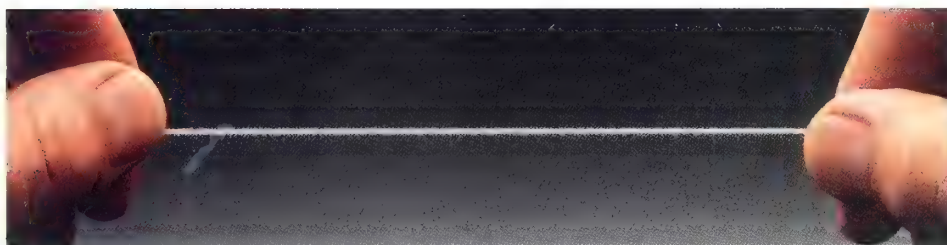


SUBARU'S "CREATIVE" SHOP SEEMED MORE INTENT ON WINNING AWARDS THAN SELLING CARS

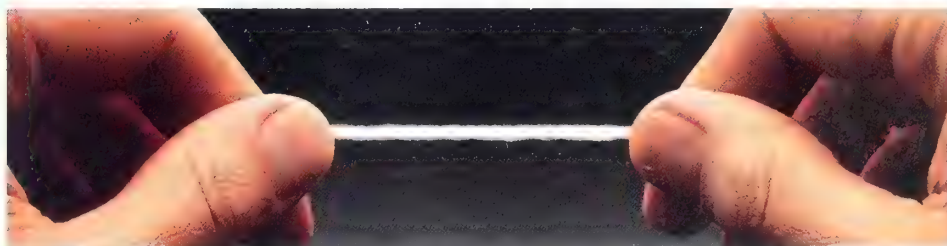
Dentists and hygienists everywhere are talking
about the following new exercise plan.



*Step 1.
Pull out a pre-measured length of new Oral-B ULTRA FLOSS.*



*Step 2.
Stretch it thin so it fits easily between your teeth.*



*Step 3.
Let ULTRA FLOSS spring back to its original thickness to brush away plaque.*

Introducing Oral-B ULTRA FLOSS, the biggest technological advance in dental floss since, well, dental floss. It's made from interwoven fibers so it stretches thin to fit easily between your teeth, then springs back to effectively remove the plaque that causes gum disease. If only every exercise program that was this good for you was this easy to do. Who else would think of it but Oral-B?



If your year begins with question marks,

it does not have to end that way.

-Greg Smith, Chief Investment Strategist, Prudential Securities

Greg Smith is more than our Chief Investment Strategist. His influence is deeply felt in the investment community. An *Institutional Investor* magazine poll has ranked him the number one market strategist since 1991. He has also ranked among the top three strategists since 1983. Greg believes there are still more than enough investment opportunities today. They're simply in different places. As the new year approaches, we're giving you his thinking about where to invest. And why.

"I expect the equity market to get off to a rocky start in 1995." While the Federal Reserve is trying to hold down inflation by raising interest rates, the government's current position is that higher rates come at the price of new jobs. This conflict between the Fed and Washington will continue to create significant uncertainty in the stock and bond markets in the coming 4 - 6 months.

"The outlook in the international market is generally more optimistic." Democratic government and free enterprise are becoming the norm throughout the world. Despite the drama unfolding in Mexico, we are still seeing a long-term strengthening of economies in virtually all of Latin America and along the Pacific Rim. With it, comes demand for roads, communication systems, power generation and rapidly expanding industrial capacity.

"You have a way to tap into these opportunities." Based on Greg's thinking, we've developed an investment strategy called Crossroads to help you focus on this growth potential. Right now, we are advising people to seek out

investments in market sectors that are benefiting from this world-wide growth. Specifically, Greg believes there are opportunities in basic industrials, capital equipment, energy and technology.

"We now know what to invest in. Crossroads tells you where." The United States economy is clearly in a growth phase. However, other parts of the world are moving faster. And with their accelerated growth, comes the opportunity for investors to achieve more significant returns over the long term.

For people who want to tap into the potential of this faster growth, but in a domestic investment, Greg Smith advises us to consider the lean, competitive multinational American companies that are helping to build these dynamic economies. Since these companies usually do business in many markets, with multiple products and services, they provide some of the advantages of diversification.

"Our analysts have identified many companies that meet our criteria." The kind of companies we suggest have already passed through the crucible of retrenchment. They're now more competitive on price, quality and service than in recent decades. For example, some of the companies currently among our Crossroads stock recommendations which may be suitable for you are: Caterpillar (CAT) 55 5/8; Cypress Semiconductor (CY) 21 3/4*; Kerr-McGee (KMG) 45 7/8; Boeing Co. (BA) 46 3/4; Asarco Inc. (AR) 28 1/2. We believe they are worth considering.

Further information is available about these stocks and other opportunities. Please call: 1-800-654-5454.



EDITED BY STEPHEN H. WILDSTROM

THE YEAR TO GO NUTS ABOUT NOTES

Back at the dawn of the personal-computer era, excited friends insisted that I had to see something called VisiCalc on an Apple II. Their inability to explain just what it was didn't dim their enthusiasm, and seeing was, indeed, believing. The spreadsheet turned out to be the program that marked the evolution of the PC from a hobbyist's toy into a vital business tool.

In the months to come, you will likely run into similar evangelism boosting Lotus Development Corp.'s Notes. Fans of the "groupware" product will not be able to tell you quite what it does, but they'll swear that it has completely changed the way they do business.

Believe them. Notes may not have the revolutionary impact of VisiCalc (or Lotus' own 1-2-3 spreadsheet), but this may be the year that the program, with about 1 million users at 4,500 companies, really breaks into the big time.

"HOLY GRAIL." Notes runs on Windows and OS/2 PCs, on Macintoshes, and on many Unix machines. It incorporates elements of e-mail, bulletin boards, and databases to give far-flung workers access to a broad variety of information. While Notes looks superficially like a messy communications program, it can change business practices in a way that led International Data Corp. to say

a 1994 study: "Notes may be the elusive Holy Grail of white-collar productivity."

What makes Notes unique, and particularly well-suited to today's business, is a technology called "replication." Computer networks have revolutionized intraoffice communications. But many people spend much of their time away from the office, disconnected from the information

chase a 250-user package whose \$62,000 price tag made it accessible to only the biggest corporations.

Notes' revised pricing policy will help. You can buy a starter kit—software for two users and a server—for \$995. Pricing for bigger networks is even more appealing: Lotus estimates that the typical cost is about \$300 per user. But the biggest impetus could come from a partnership between Lotus and AT&T. Network Notes, now being field-tested, will make it simple to extend a Notes network beyond corporate walls, linking Notes-based companies with their customers and vendors without them having to solve the tough problems of getting

their networks talking directly to each other.

PEEK-PROOF. In one test, software retailer Egghead Inc. is using Network Notes to handle orders from its corporate customers. Compaq Computer Corp. is using the system to give product and price information to customers. Notes' security features ensure that prying eyes cannot find out how much the customers are paying.

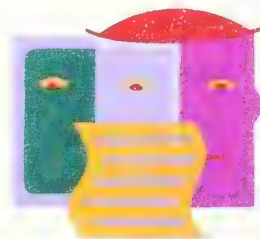
Notes is attracting some heavyweight competition. Microsoft's oft-delayed Exchange Server will offer many of the same features. Novell is trying to integrate Netware with the Word Perfect GroupWise message-handling product it acquired last year. Banyan Systems Inc. is building a rival it calls BeyondWare. But Notes, with an enhanced version 4.0 now in final testing, enjoys a huge headstart. So business computer users who need to work more closely with their colleagues, vendors, or customers should check Notes out today. *S.W.*

BULLETIN BOARD

SOFTWARE

XEROX IS IN GOOD FORM

Computerized forms have greatly eased paperwork chores. But there are times when, for legal or practical reasons, a form has to be printed out for revision. And once the document, say a benefits-change form, is out of the computer, reentering changes requires



slow, costly clerical work.

Xerox Corp.'s SmartPaper technology could automate the process. It preserves the old data in a series of fine lines that look like a gray box on the printed page. Scanning the form back into the computer automatically updates the stored record with the new choices the employee makes by checking boxes. Xerox Desktop Document Systems (800 248-6550) is licensing the technology to software developers.

PDAS

WRITE IT OR TYPE IT

The market may be slow to take off, but choices in personal digital assistants are growing. The latest entry, priced from \$750 up, is Sharp Corp.'s Zaurus (800 237-4277). It features a miniature keyboard and the ability to store handwritten notes—but not convert the notes to computer text. In case you're wondering, the name was chosen to be "language neutral," or meaningless in any language.

Cellular Phone

Fax

E-Mail

Cellular Pager

Address Book

Calendar

Appointment Scheduler

Calculator

World Time Clock

Paperless Note Pad

Handwriting Annotation

Standard and Predictive Keyboards

Help Functions

Now Available!



Simon Says "Hello."

Simon has arrived and it's as revolutionary as you've heard. Say hello to the world's first personal cellular communicator that puts all your mobile business tools into one small, handheld package. It's easy to use, affordable and it's wireless! So it goes where you go — works where you work. Say hello to Simon. It's simply innovative.

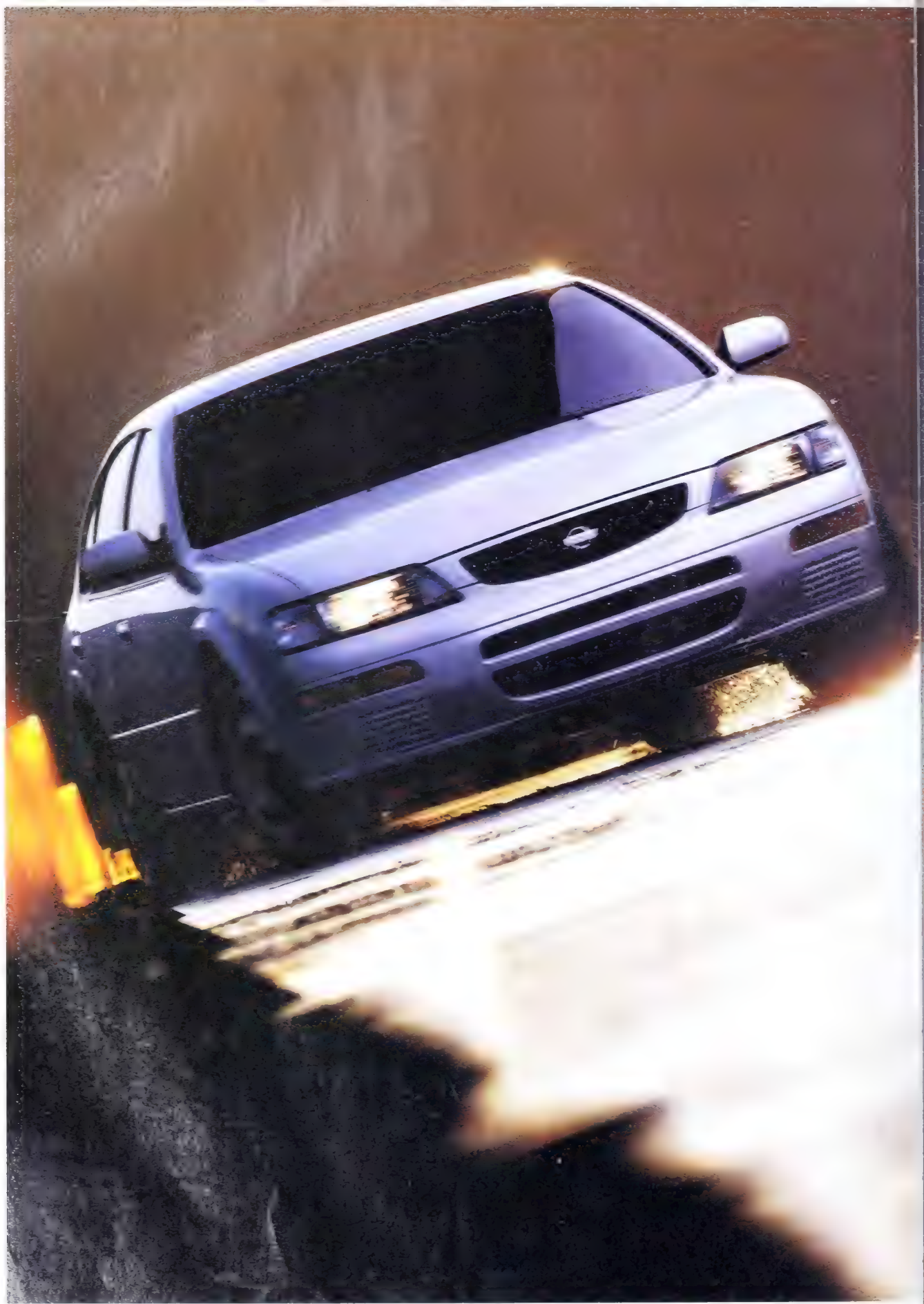
Call 1-800-SIMON SAYS. And Let BellSouth Simplify Your Mobile Communications.

SimonTM
Mobile Communications Made Simple

From **BELLSOUTH**
Designed by IBM



Simon Specifications - Size: 8" x 2.5" x 1.5"; Weight: 18 oz.



Only a car this quiet could make so much noise.

seems the automotive press can't stop talking about the new Maxima. • Take Motor Trend, for example, who after their first road test concluded, "We're impressed that the Maxima offers the comfort and quiet once reserved for luxury-channel cars." • They went on to add, "This Nissan ranks among the best values in a luxo/performance sedan. Acura, BMW and the rest need now be concerned." • The Maxima made such an impression on them, they named it the 1995 Motor Trend Import Car of the Year. • No small feat when you consider that the field included contenders from Porsche, BMW and Lexus. • But the Maxima beat all of them. Thanks in part to a potent V6 engine that blasts from 0-60 in a mere 6.6 seconds. Yet, this same engine delivers the fuel economy of a miserly 4-cylinder compact.** • As for handling, the Maxima can easily outmaneuver many expensive European sedans costing twice as much. • And speaking of cost, the Maxima has a starting price of under \$20,000.† Which, much to the chagrin of our competitors, isn't something we're going to keep quiet about.*

To learn more, call 1-800-335-4680. Or visit your nearest Nissan Dealer for a test drive.

The New Maxima. Motor Trend's 1995 Import Car of the Year.



It's time to expect more from a car.™

n Motor Corporation U.S.A. Smart people always read the fine print. And they always wear their seat belts. *Motor Trend, June 1994 **1995 EPA fuel economy estimates 22 miles per gallon city/27 miles per gallon highway with 5-speed. Use these estimates for comparison only. Actual mileage may vary with driving conditions. †Mileage comparison versus Subaru Legacy AWD 5-speed. ‡Manufacturer's Suggested Retail Price for 1995 Maxima GXE excluding taxes, title, license, destination charges, options and locally required equipment. GLE model shown. Dealer sets actual prices. Prices are subject to change. In Canada, call 1-800-387-0122.

BY ROBERT KUTTNER

REWRITE THE REGULATORY RULEBOOK—DON'T TEAR IT UP



FINESSE:
The challenge facing the new Congress: How to dismantle stultifying bureaucratic rules while continuing to protect the public interest

With the Republican takeover of Congress, deregulation is back in vogue. However, it isn't just bureaucratic pointy-heads who dream up health, safety, and environmental laws. A great many regulations come into being because some private-sector excess—tainted meats, lethal drugs, maimed workers, polluted streams, bilked investors—leads to a public outcry and a demand for remedy. Moreover, in the absence of regulations protecting health, safety, and the environment, individuals seek recompense through costly private litigation.

Still, bureaucratic regulation tends to ossify, and so regulatory reform is not entirely miscast. Since the late 1970s, both political parties have supported partial deregulation of airlines, trucking, natural gas, telecommunications, and banking—with mixed results. And lately, “marketlike” regulation has sought to harness market forces to do what would otherwise be done bureaucratically.

A pleasing example is the offer of a free ticket to a passenger willing to give up a seat on an overbooked flight. This minimarket allows airlines to book flights tightly while still guaranteeing that tickets will be honored. Another example is the trading of pollution rights, allowing industries to bank savings in their emissions of pollutants and to buy and sell them as necessary. Still another is the recent auction of the broadcast spectrum for the next generation of wireless communications devices.

FIRST THINGS FIRST. Yet these contrived markets in bumping rights, pollution rights, and broadcast licenses, while ingenious and often efficient, are neither simple alternatives to regulation nor free markets. They're the products of government regulation. No airline would give away tickets unless it was first prohibited from bumping. Nor would there be a market in pollution rights without government limits on allowable emissions.

A revolution is also occurring in the regulation of what were once viewed as natural monopolies. Public utilities used to receive a franchise to be the sole local supplier. In return, they had to provide virtually universal service, at regulated rates, and were guaranteed a normal operating profit. However, a generation of economic analysis has demonstrated that this kind of regulation tolerates inefficiencies, retards innovation, and often promotes investment motivated mainly by

the desire to increase the rate base. New technology adds to the allure of deregulation. There is no longer a technical reason why the phone company or the electric company need be a monopoly.

Yet as long as we want a local provider-of-last-resort, required to supply phone service or electricity to any willing customer, complete deregulation is out of the question. The Federal Communications Commission, the Federal Energy Regulatory Commission, and state public utilities commissions are all grappling with how to deal with the oxymoronic world of pro-competitive regulation.

BALANCING ACT. Consider the dilemma of reconciling competition with partial rate regulation. The local Baby Bell, for example, is stuck with an expensive “installed base” of cables, switching devices, and other capital equipment. It keeps the local grid operating, and its rates are based on its costs. If new competitors are allowed in willy-nilly, they'll underprice the Baby Bell and render it uneconomic. But if the Bell keeps its monopoly, the consumer will be denied available choices.

There are pro-competitive solutions to such dilemmas, but each requires ground rules—namely, regulation. Lately, there has been a wave of creative regulatory reform at both state and federal levels, relying on such devices as free competition under price caps and mandated cost-sharing by competitors. Such reforms are designed to reconcile the contradictory goals of universal service and increased competition—but they hardly constitute a perfect free market.

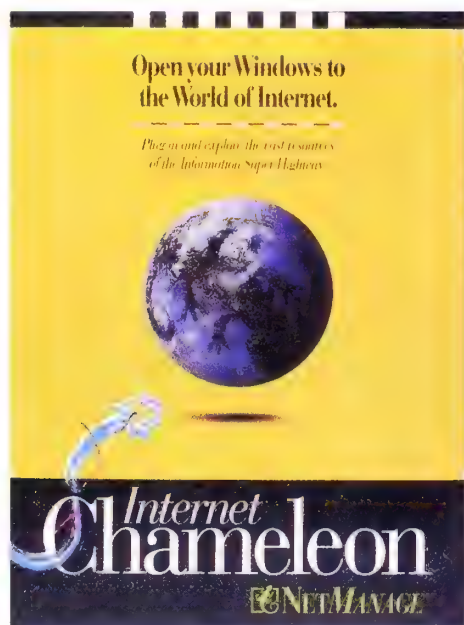
Conservative economic theory holds public-interest regulation to be a hopeless enterprise. Regulators are said to be captives of special interest groups, or “rent-seekers,” interested only in expanding their own empires. But those same corrupting political pressures operate in a world of deregulation—witness the savings-and-loan scandal. Even a market economy requires rules, and the rule-setters need to be as creative and public-minded as possible.

In fact, federal and state regulatory agencies have done very well in rising to the challenge of reinventing regulatory systems to encourage competition and technical dynamism while still protecting a broad public interest. It would be a shame if this sensible pragmatism gave way to a dogmatic onslaught of deregulation.

Robert Kuttner is co-editor of *The American Prospect* and author of *The End of Laissez-Faire*.

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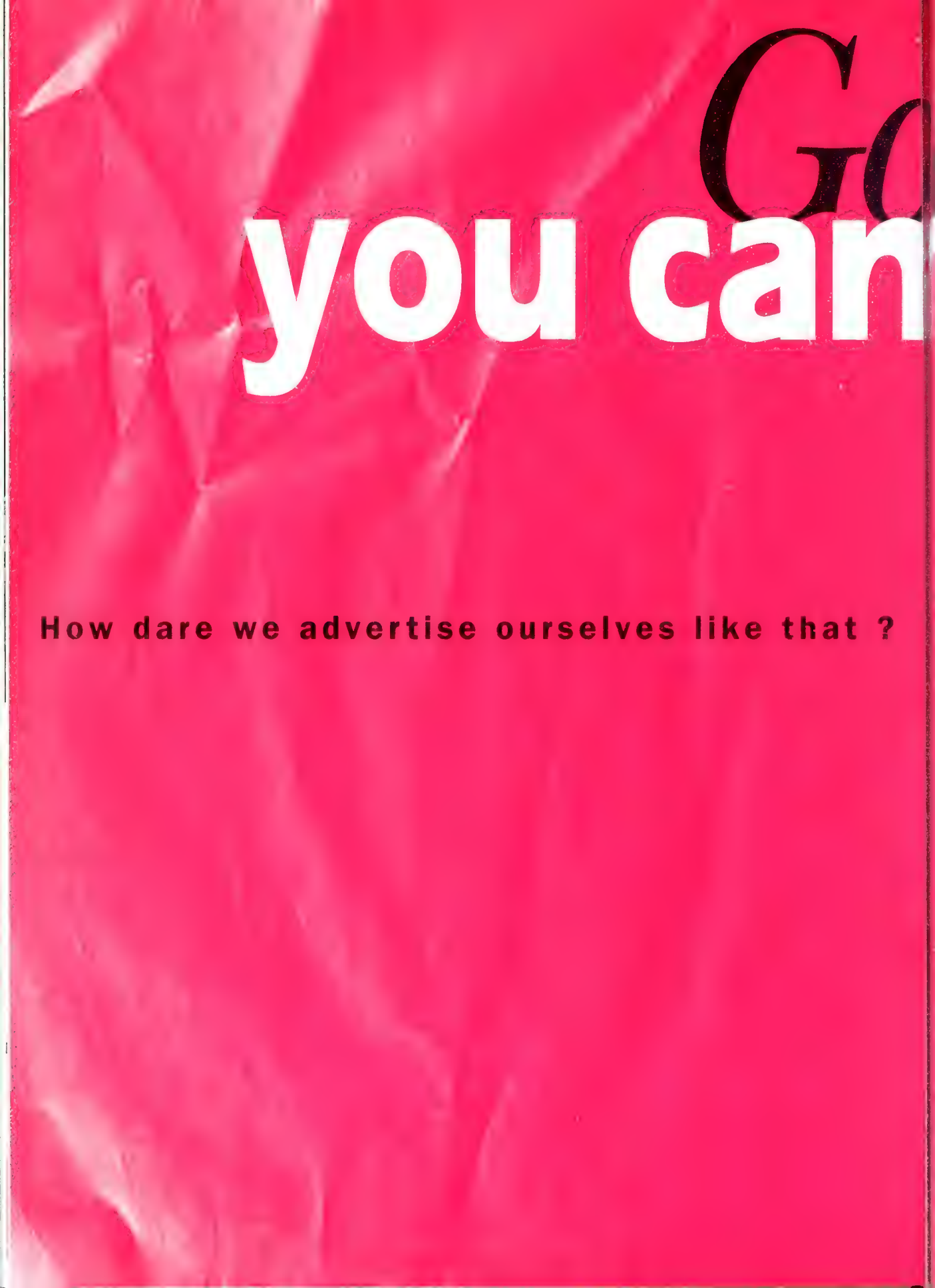


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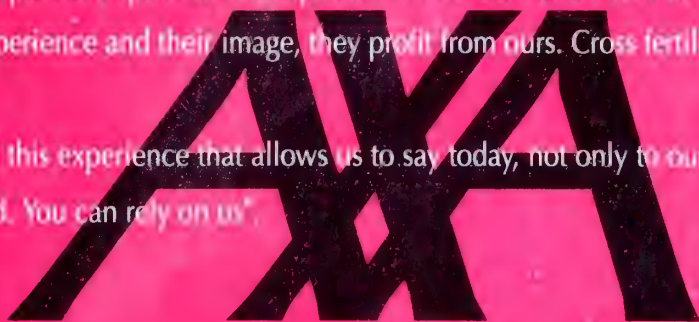
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INSURANCE & INVESTMENT

BY GENE KORETZ

FALLEN EMPIRE, FALLING PEOPLE

Former Soviet populations dwindle

Nowhere is the economic and political chaos enveloping the former Soviet Union more evident than in its impact on demographic data. In a new Population Reference Bureau study, demographer Carl Haub notes that as late as 1988, the entire Soviet Union had expanding populations and birth rates promising long-term growth.

Now, however, fertility rates have fallen in every former republic—plunging far below replacement level in Russia, Belarus, Ukraine, Estonia, Latvia, and Lithuania. In Russia, which has half of the former Soviet Union's population, more than two-thirds of pregnancies are aborted.

Infant deaths and overall mortality rates have also risen. The starkest trend has occurred in Russia, where male life expectancy fell to only 58.9 years in 1993, the lowest of any industrial nation. In 1993, five of the seven European republics, representing over 70% of the former Soviet Union's people, suffered population declines.

WHAT TO EXPECT IF WELFARE ENDS

Who will hire former recipients?

A popular view these days is that eliminating welfare for able-bodied people would not only save taxpayer dollars but would also free recipients from the debilitating trap of dependency and spur them to become self-reliant.

A new study by Sandra K. Danziger and Sherrie A. Kossoudji of the University of Michigan, however, underscores the severe employment problems facing welfare recipients. In 1991, the state of Michigan did exactly what some welfare critics have advocated: Facing a budget deficit, it abruptly terminated

General Assistance (GA), a program that had been providing a maximum of \$160 a month to 80,000 poor working-age jobless adults with no dependent children.

The researchers looked at how a sample of presumably "able-bodied" recipients fared after losing their cash assistance (they continued to receive food stamps and medical coverage). The good news is that nearly two years after GA ended, almost 20% had regular jobs—with an average gross pay of \$650 a month. Some of these, of course, would have found work even if the GA program had not been terminated.

Of the 80% or so of former recipients who remained unemployed, on the other hand, almost a fifth were in such poor health that they were able to qualify for disability assistance. The rest managed to scrape by with help from family and friends, odd jobs, and recourse to programs like homeless shelters and food pantries. In general, their meager living standards declined.

Why didn't more people wind up with jobs? The study reports that 58% of ex-recipients had chronic health problems, 40% were over age 40, half were high-school dropouts, over half lived in minority-concentrated inner cities, and 25% lacked work experience. Those who found jobs tended to be younger, healthier, and better educated, and to live in less blighted areas.

HOW NON-HMO DOCS COMPETE

They cut some fees, but not income

Competition may have less of a moderating effect on health-care outlays than many observers believe. Take the case of doctors' office-visit fees. Economist Laurence C. Baker of Stanford University reasoned that the growth of health-maintenance organizations might induce independent doctors to cut fees in order to compete. And in a recent study, he did find that greater HMO market shares in a region were associated with appreciably lower office fees among non-HMO practitioners.

The catch: The study also indicated that the independent physicians managed to maintain their incomes despite their lower office fees. Since they didn't work more hours or see more patients than doctors in areas lacking HMOs, Baker theorizes that they may have offset their lower office fees by raising fees for tests and procedures or by stressing services with high profit margins.

WHY THE CRY FOR TAX RELIEF?

Slack income growth is the spur

The consensus among economists these days is that middle-class tax relief this year is likely to be more cosmetic than real. As Bruce Steinberg of Merrill Lynch & Co. notes, entitlements (mostly Social Security and Medicare), interest payments, and defense absorb about 88% of the federal budget.

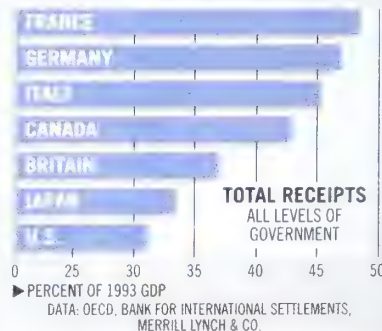
Excluding Medicaid, welfare programs take only 7% of federal spending. And the modest 12% devoted to such discretionary outlays as education, the environment, and highways is already the lowest share of federal spending and gross domestic product in 40 years.

In light of these budgetary constraints, the need to offset tax cuts with spending cuts, and Republican pledges to move toward a balanced budget, anything more than very modest tax relief for the middle class seems problematic. Indeed, an irony of the current situation, observes Steinberg, is that the U.S. still enjoys the lowest tax bite among industrial nations (chart). Moreover, the federal tax burden has actually been "incredibly stable at about 19% of gross domestic product for three decades."

So why the tax-cutting frenzy? The answer seems to be continuing widespread economic malaise. The government reports that men aged 25 to 54 who lost and then found full-time jobs in the early 1990s suffered average real earnings declines of 20%. From 1989 through 1993, median real household income fell steadily by a cumulative 7%.

Unable to influence the economy's inability to raise average incomes in recent years, legislators are turning to the one economic lever they do control: the power to reduce taxes.

GUESS WHOSE TAXES ARE LOWEST

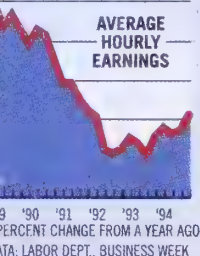


IF THIS KEEPS UP, THE FED MAY COME DOWN TOO HARD

U.S. ECONOMY

After nearly a year of tightening the screws, the Federal Reserve stands at a critical juncture. The current round of interest rate hikes has reached the point where the outlook boils down to two most likely scenarios. One, the Fed eases the economy enough to curtail price pressures but without precipitating a recession. Or two, the Fed over-tightens, ushering in a period of stagnation—or worse. The trouble is, the chances for scenario No. 2 just got better. Maybe not this year, but by 1996. The vitality evident in the December employment report argues that fourth-quarter economic growth was the fastest of 1994, suggesting that past Fed tightening still has not had its desired effect. The stronger the economy, the more the Fed will be inclined to lean against it, and the greater the chances the central bank will push too hard.

WAGE GROWTH STARTS TO CREEP UP



Growth is already drifting upward (chart). The rate increase, expected to be anywhere from a half to a full point, will at least double the level of short-term rates since Feb. 4, 1994. In the past, such an aggressive move has always yielded either a sharp slowdown or outright recession.

NOT HIT the panic button just yet, though. There are some good reasons to believe that the economy will slow down before the Fed goes too far. Consumers hold the key. True, job growth is strong, but households are unable to maintain the heady pace of buying they posted in the year's second half. Higher rates are already crimping housing, and that will rein in demand for household durable goods. Both were big contributors to growth in 1994. Also, households are starting to stretch their credit cards at a time when savings are very low. Consumers added a huge \$12.9 billion to their installment debt in November. Revolving debt, mainly credit cards, shot up by \$10 billion. Debt loads have surged 15.1% from a year

ago, a pace not seen since the credit binge of the mid-1980s, and the ratio of debt to aftertax income is back up to 17.8% from a low of 15.2% two years ago.

The main worry right now is that consumers—and the rest of the economy—will continue to barrel ahead, generating the very price pressures that the Fed wants to preempt. So far, the news from the price indexes remains good, but some acceleration in inflation in 1995 looks inevitable.

For finished factory goods, the producer price index rose a mild 0.2% in December. The core index, which excludes energy and food to give a better tracking of how economic forces are influencing prices, was also up 0.2%. For all of 1994, finished-goods inflation was a mere 1.7%.

And the consumer price index increased a modest 0.2% in December, bringing 1994 consumer inflation to only 2.7%, with many categories of goods and services experiencing slowdowns (table). For the third consecutive year, the CPI has risen less than 3%, something that hasn't happened since the mid-1960s. Moreover, core inflation ended up at only 2.6% last year, the lowest since 1965.

But now, worries about rising capacity-utilization rates and tightening labor markets are beginning to give way to more direct signs of inflation. For example, inflation for intermediate goods—such as paper, fabrics, and motors—from which finished goods are made, has picked up sharply in recent months. Prices of such goods, excluding energy and food, are up 5.1% from a year ago, compared with a 1% pace back in April.

History shows that it takes about a year for increases in intermediate-goods prices to work their way into finished goods. So far, however, that pass-through effect is being limited by opposition from final producers and consumers.

Buyer resistance to higher prices, fanned by fierce competition, is forcing retailers to the cheapest supplier. That's the key reason for last year's drop in apparel prices. And many producers are fighting—or swallowing—higher materials costs for fear of losing business.

STILL, WAGES are far more important to the inflation process than the bill for materials, because labor costs are three-fourths of the economy's cost structure. That's why

INFLATION SLOWS FOR MANY PRODUCTS		
PERCENT CHANGE, DECEMBER TO DECEMBER		
	1993	1994
FOOD	2.7%	2.7%
HOUSING	2.7	2.2
APPAREL	0.9	-1.6
TRANSPORTATION	2.4	3.8
MEDICAL CARE	5.4	4.9
ENTERTAINMENT	2.8	2.3
MISCELLANEOUS	2.7	4.2
ALL ITEMS	2.7	2.7
CORE*	3.2	2.6
*EXCLUDING ENERGY AND FOOD		
DATA: LABOR DEPT., BUSINESS WEEK		

the December labor-market report is a bit worrisome. It not only suggests that growth in fourth-quarter gross domestic product could have easily topped 4%, perhaps reaching 5%. It also shows that job growth was unrelentingly strong heading into 1995, at a time when wage gains are beginning to show some upward tilt.

Given last quarter's strength, it's now apparent that real GDP has exceeded the Fed's measure of potential GDP—the output that is possible when all resources are fully utilized. That suggests that demand for goods and services is outpacing the economy's ability to produce them. That gap usually is corrected by higher wages and prices.

That's why monetary policy is entering such a critical stage. The longer the economy grows faster than its potential noninflationary rate of 2.5% or so, the further the Fed will have to push growth below that rate in order to wring out price pressures.

If so, policy makers attempting a soft landing face a problem. It is easier to avoid injury if you maintain an economic cruising speed of 2%-2.5%. Ratchet the velocity down to 1% or less, and the chances of a crash rise sharply. At the very least, unemployment starts to rise.

DECEMBER'S JOB DATA gave no hint that growth was slowing. Businesses added 256,000 workers to their payrolls last month, and the November jump was revised upward by 138,000, for a hike of 488,000. That was the

largest monthly gain in seven years. The December rise was broad, led by services, retailing, and manufacturing.

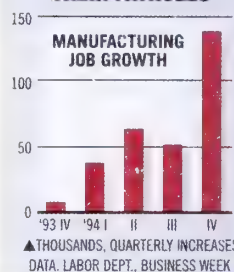
Factories added 54,000 new slots last month. The three-month string of sizable gains indicates an acceleration in the hiring uptrend that began about a year ago (chart). Indeed, the three-month increase is the most since 1987.

As a result of tighter labor markets, wages are starting to grow a bit faster. Average hourly earnings rose a modest 0.3% in December, but for the fourth quarter, they increased at an annual rate of 4%, the fastest quarterly advance in 3½ years. Looking at the annual trend, hourly pay has risen 2.8% from a year ago, up from its low of 2.3% hit in 1993.

The good news for consumers is more income to spend. The boost in hourly earnings last quarter, plus longer hours and the surge in jobs, means that fourth-quarter personal income posted a big gain.

However, today's festive mood might turn funereal. If consumers don't brake their spending in the first half, the economy will keep charging ahead faster than the Fed wants. And the Fed will keep jacking up interest rates until growth slows—to one degree or another.

FACTORIES BEEF UP THEIR PAYROLLS



LATIN AMERICA

MEXICO'S QUAKE ROCKS ARGENTINA

Who's next? Burned by Mexico, investors even in more stable emerging markets such as Argentina are wary of holding securities that would fall in price if another country devalues its currency. So financial markets in Buenos Aires and elsewhere are being hammered.

Since Dec. 20, Argentina's blue-chip stocks are down 27%, including a 9.6% crash on Jan. 10 (chart). Interest rates have shot up, but withdrawals from smaller banks are straining the banking system. To calm big investors, Finance Minister Domingo Cavallo rushed to New York on Jan. 10.

Cavallo and others are dead set against a devaluation, because it

could bring back hyperinflation. Also, the country's Convertibility Law links the Argentine peso to the U.S. dollar, and the central bank must hold dollar and gold reserves equal to the amount of pesos in circulation.

Argentina's current turmoil hits just as its 1991 reforms are bearing fruit. It has torn down trade barriers, raised capital spending, and amassed a healthy level of foreign reserves. The payoff: The economy grew 8% in 1994, and inflation fell to a 51-year low of 3.9%.

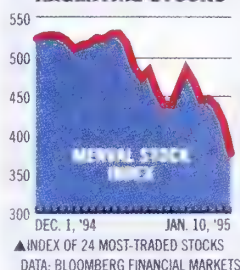
Still, Argentina had some trouble spots even before December. Surging imports and foreign-capital needs had pushed its current-ac-

count balance into the red. And its fiscal finances slipped into deficit in 1994. Cavallo projects a 1995 surplus, but investors aren't sure.

In lieu of devaluation, Argentina will have to choose another strategy to save its financial system. It could effectively dollarize its economy. Or, to keep capital within Argentina, the government can hold interest rates high. Credit restraints would probably ease foreign-investor jitters, but at the cost of a recession in a country where the unemployment rate is already 12%.

The May elections complicate policy-making. President Carlos Menem was expected to base his reelection bid on the success of his economic reforms. But the latest snafu shows the reach of Mexico's shock waves.

INVESTORS HAMMER ARGENTINE STOCKS



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General Electric Co. did it. IBM is doing it. Eastman Kodak Co. is forever trying. And now, in a head-on collision of the unthinkable and the unmanageable, the vast enterprise known as Uncle Sam Inc. is about to join the restructuring revolution.

The U.S. government is on the brink of its first serious reorganization since the New Deal—pushed there, fittingly, by the threat of wholesale customer rebellion. After enduring years of shoddy service, late deliveries, high prices, and surly sales help, Americans bellowed “Enough!” on Nov. 8. “The message of the election is that the American people think the federal government is too big and too intrusive and messes with their lives,” says Of-

fice of Management & Budget Director Alice M. Rivlin.

AMBIVALENT. Voter anger at government, of course, masks some underlying ambivalence: While most agree that Washington has its problems, relatively few citizens actually favor the demolition of specific agencies or the elimination of services. Over the coming months, that reality will provide political roots for a fractious, defining debate on what government should be. How big? How intrusive? Who will deliver services? And who will pay?

Although Democrats and Republicans have greatly differing visions of government's role, both want to create a smaller, nimbler, more market-

WHERE THE AX COULD FALL...

HOUSING The Housing & Urban Development Dept. already plans to cut 37% of its workers. Republicans want to eliminate the agency entirely. The White House would spin off the Federal Housing Administration into a semiautonomous corporation and shift public-housing funds into vouchers.

AIRWAYS The costs of the air-traffic-control system will be shifted from taxpayers to air travelers. The system will be turned over to a private contractor or run as a quasigovernmental entity.

JOB TRAINING Of 154 existing programs, the White House wants to consolidate 50, turning them into voucher schemes that will allow people to buy training from private providers. Republicans may cut the programs entirely.

driven bureaucracy. Republicans are putting together a massive hit list of federal programs, agencies, and Cabinet departments. Among their possible targets: the Departments of Commerce, Housing & Urban Development, and Education—though GOP legislators are divided on how far this revolution actually should go.

Spurred by the Democrats' rout, President Clinton has directed Vice-President Al Gore to greatly expand the Administration's “Reinventing Government” (REGO) campaign. Agencies, Gore says, will have to “justify why they should continue to exist at all” (page 40). So far, the White House has proposed reorganizing—but not eliminating—five federal agencies, among them Transportation and HUD. Clinton also proposes turning over to the private sector some government enterprises, such as the Federal

Housing Administration. And he wants to shift responsibility for others, such as some low-income housing and transportation programs, to the states.

Ultimately, though, Democrats' fundamental faith in a broad governmental role will yield to Republican deconstruction. The next two years are likely to witness a

DOWNSIZING

Much of the New Deal may be dismantled as

of reverse New Deal that will tear many of the props supporting the safety net and, indeed, much of the acquired by the federal government in years of Reaganism. The most radical proposals will be muted in the face of special-interest politics, but a plethora of programs will be shifted to states, cities, counties—closer, as it were, to the customer. And many services and subsidies Americans take for granted will be eliminated. It will be time, in other words, to learn what we can live without.

To which Corporate America says: It's about time.

"Businesses have been restructuring for the last decade," says John Roach, CEO of Tandy Corp. "It's now time for the government to start." Both Clinton and the GOP, in fact, have turned to business for tips on how to

improve management of government agencies. House Speaker Newt Gingrich (R-Ga.) has met with such top chief executives as John W. Snow of CSX Corp. and International Paper Co.'s John A. Georges; Gore has huddled with Xerox Corp.'s Paul A. Allaire and Frederick W. Smith of Federal Express

...AT UNCLE SAM INC.

WELFARE Benefits will be cut. More important, states will assume a greater role in designing and paying for the program, producing vastly different schemes from state to state.

REGULATION Federal rules will be streamlined. Cities and states won't have to comply with federal laws unless Washington helps pay the tab. Some agencies, such as the Interstate Commerce Commission, will be abolished. The Food & Drug Administration will be pressured to speed up approvals.

MISCELLANEOUS SUBSIDIES Agriculture payments are likely to be trimmed, as are incentives from the Small Business Administration. Regional power-marketing agencies will be sold off, increasing electric costs in much of the West.

Corp. "Things that are making American business more competitive can be applied to the federal government," says the Speaker. "Government has a lot to learn from the private sector."

PRICEY FREEDOM. The feds have much to learn, too, from their colleagues in statehouses and city halls. In the past few years, creative politicians such as Philadelphia Mayor Edward G. Rendell and Colorado Governor Roy Romer have begun implementing a new brand of "entrepreneurial government" that stresses market incentives, partnerships with business, and privatization. Milwaukee is experimenting with "total quality improvement," and Chicago, Indianapolis, and other cities are privatizing everything from golf-course

maintenance to parking-fine collection (boxes, beginning on page 36).

Washington's attempt at decentralization will give states even more freedom, providing them with the latitude to experiment with health care, welfare, and other services. Ironically, though, it also will increase the pressure on those governments, as responsibility for running former federal programs shifts downward.

The result could be wildly differing levels of services from one jurisdiction to another and a maze of varying regulations for interstate corporations to navigate. And be forewarned: It could mean higher overall tax bills—especially if Washington

GOVERNMENT

both parties race to reshape Washington

UTAH

Michael O. Leavitt



Frustrated by federal intrusion into state affairs, Republican Governor Michael Leavitt of Utah is spearheading efforts to give states more autonomy.

His brainchild: a Conference of the States for this fall that will propose constitutional amendments aimed at what he calls a "long-term leveling of power" between Washington and the hinterlands. He came up with the idea two years ago, and fellow governors were enthusiastic. One amendment would let states repeal a federal law

when two-thirds of state legislatures agree. That would require congressional approval—but a refusal from Capitol Hill, says Leavitt, "would illustrate an arrogance that would be intolerable."

cuts funding to the states even as it passes on new responsibilities. In the past two decades, in fact, state and local payrolls have grown far faster than Uncle Sam's, as demand for health care, education, and prisons has ballooned (charts). "Anyone who thinks that we can do all these things without state and local taxes increasing is being unrealistic," says Republican Governor George V. Voinovich of Ohio.

Downsizing government will prove a difficult balancing act indeed. According to a new BUSINESS WEEK/Harris Poll, a majority of Americans favors shifting more responsibility for a wide range of federal programs to the states. But only 40% would pay higher state taxes for those services. And most Americans still want to keep all existing federal agencies (page 42). Says Democratic pollster Mark Mellman: "When you ask people if government spending should be cut, they say: 'Absolutely.' But there's not a majority for cutting any specific program in this country."

Even so, some cuts are all but certain. Federal subsidies for the arts, agriculture, science, and low-income housing will be curtailed. The air-traffic-control system may be turned over to a private corporation. Stringent consumer-protection rules and a host of other federal regulations will be reduced. The crazy quilt of overlapping U.S. programs will be consolidated, and the federal workforce will be cut by more than 10%. Says Senate Government Affairs Committee Chairman William V. Roth (R-Del.): "We've got to bring this Rube Goldberg hodgepodge into the 21st century."

The coming revolution will provide an ex-

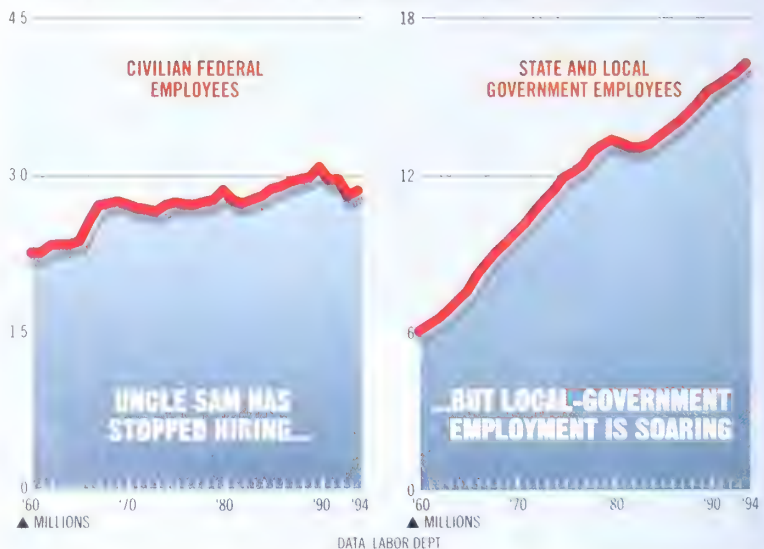
traordinary leadership test for both the beleaguered Clinton and the confident new barons of the Republican Party. It will give the President perhaps his last chance to define his vision of government. Is he the ex-governor who thinks—as he often tells friends—that Washington would mess up a one-car funeral? Or does he believe in the kind of centralized planning that lay at the heart of his health-care-reform proposal?

"A BLOWTORCH." And will the GOP be the Robin Hood of the country-club set—taking from the poor and "cultural elites" and giving to its constituents in the form of tax cuts? Or will the New Jeffersonians slash equitably, taking the knife to government subsidies that help favored industries and the wealthy, too? Just as important, will congressional Republicans be willing to give up power to the states? "I we're not careful," frets GOP pollster Anthony Fabrizio, "we'll be seen as protecting powerful interests and corporate welfare while eviscerating the poor."

Indeed, any business executive who has managed a corporate restructuring knows that urgency and bold action, not tentative steps, are what turn organizations around. "You need more than a spark, you need a blowtorch," says retired Continental Bank Corp. Chairman Thomas C. Theobald, who saved the crippled bank in part by cutting its workforce by 60%.

Certainly, Washington needs more than incremental improvements. The balanced budget amendment that Congress is expected to approve and send to the states for adoption within the next few weeks would require more than \$1 trillion

WHERE IS DOWNSIZING REALLY NEEDED?



Corporate America could feel the downsizing, since ma

ts from planned spending. Even without fiscal pressure, too many federal programs obsolete or redundant. It is hard to justify, for example, 154 separate job-training programs, or a half-dozen export-promotion operations, or 600 grant programs, 75% of which contribute less than \$50 million each annually. Downsizing experts believe that the federal bureaucrats should be removed from such programs as public housing, allowing local governments to solve local housing problems themselves. Another option: giving the \$17 billion by the feds on public-housing construction to other subsidies directed to the poor in the form of housing vouchers, allowing them to choose their own choices.

Another prime cutback candidate: special-interest business subsidies known as "corporate welfare." Why should the Small Business Administration, for example, spend \$600 million subsidizing a handful of companies to the exclusion of their competitors?

The federal government does have a vital role to play in interstate commerce, national defense, civil rights, and environmental regulation, as well as in regulating civil rights. But even those missions can be handled more efficiently by far fewer people. For instance, public defense could be managed by a single agency rather than by too many of often-competing offices. And by reforming anti-Civil Service laws, bureaucrats could be evaluated and, if needed, fired—just like their private-sector counterparts. Clinton has started down that road with his proposals to reorganize Transportation, Energy, HUD, the General Services Administration, and the Office of Personnel Management. HUD Secretary Henry G. Cisneros, for example, restructured his department after studying a reorganization



OREGON

Vera Katz

There's a new crime-fighting strategy in Portland, Ore. The cops are the same, but the city is trying to be more nimble by shifting resources to where they do the most good. That means curbing car theft, say, by targeting the city's 10 most vulnerable neighborhoods.

The strategy hasn't met expectations, but Mayor Vera Katz, a Democrat, is relying on Oregon's benchmarking system to help her reassess goals: "We're far more proactive... rather than just letting programs continue or adding more money." Because benchmarking stresses cooperation among local governments, she can work closely with the county to defeat bad guys.



at PepsiCo Inc. HUD eliminated 10 regional managers and gave its field officers more power to set policy. Cisneros figures he can cut his 11,900-strong workforce by 4,400 over five years, in part by turning some funds over to cities and states and the rest to poor families in the form of vouchers. "We literally reinvented HUD as a right-side-up organization, not a top-down organization," says Cisneros.

Such changes have cut across Washington. Thanks to attrition and a generous buyout program, federal employment has been trimmed by some 100,000 jobs since 1993. Government procurement has been streamlined by giving line managers authority to buy goods off the shelf rather than relying on costly centralized-purchasing requirements. At the GSA, which is responsible for federal buying and real estate, Administrator Roger W. Johnson—the former CEO of Western Digital Corp.—thinks he can save up to \$20 billion over five years. For starters, he'd spin off operations to private companies owned by ex-employees.

BENCHMARKS. In his fiscal 1996 budget, Clinton also will propose consolidating 105 Public Health Service programs—including podiatric education and dentistry for AIDS patients—into seven supergrants to states. That would allow governors to decide how to spend federal health dollars with less interference from Washington. The President also wants to consolidate 50 job-training programs. In their place, he'll provide workers with up to \$3,000 in vouchers to improve skills. "People want opportunities from government," says Assistant Labor Secretary Douglas D. Ross. "But they don't want to go through bureaucratic third parties."

Washington also will move toward instituting benchmarks to evaluate effectiveness, building on a new system designed by Oregon. There, state administrators have promised, for exam-

ARIZONA

Frank A. Fairbanks

Phoenix' Frank Fairbanks ranks near the top of most people's list of best city managers. Under his leadership, citizens say most city services have improved, and costs are down. When Fairbanks slashed 490 jobs in 1990, for example, he told departments to rethink processes to reduce hassles for residents.

"I don't see my job as being the person who invents every good idea," he says. The city has saved \$7.9 million by adopting suggestions of employees, who keep 10% of savings. The appointed manager also is big on competitive bidding for services, a program Phoenix has pioneered for 15 years. City departments, competing with private contractors, now win 40% of the bids.



panies are as reliant on handouts as welfare mothers

PENNSYLVANIA

Edward G. Rendell



the federal bureaucracy." But he worries about losing housing and mass-transit assistance. Major reductions, he says, "would be extremely difficult" for his city to handle.

The maverick Democrat has turned around Philadelphia. When Edward Rendell became mayor three years ago, the city deficit was \$200 million. He has since balanced the budget without raising taxes, in part by privatizing 26 city services and cutting the workforce by 5%.

Rendell favors a new urban agenda, featuring targeted federal tax credits and capital-gains tax cuts. He agrees it's time for the federal government to slim down: "There's no question you can save billions of dollars by cutting

ple, to actually cut teen-pregnancy rates in half by 2000 in return for strings-free Washington aid. Now, led by Gore and Rivlin, the White House is pressing for similar accountability. OMB is quietly demanding that agencies justify future budget requests by showing results. And in the spring, the White House will propose a new regulatory scheme that would free businesses from explicit rules as long as they meet overall performance goals.

Such changes may be just the beginning. Gore has asked for a bottom-up review of every department and agency. Vows one Administration official: "We're going to see what should be terminated, consolidated, devolved to the states, or privatized." GOP demolition experts want to go much further. Roth would slash the 14 Cabinet departments by as many as half. Senate Budget Committee Chairman Pete V. Domenici (R-N.M.) vows to kill at least 100 programs. And House Budget Committee Chairman John R. Kasich (R-Ohio) is compiling his own hit list—including the departments of Commerce, Education, Energy, and Interior.

Republican reformers are just beginning to fathom the political and legal complexities of abolishing entire agencies. For instance, a department can't be killed before the hundreds of laws that govern its programs are changed. "This isn't as easy as a lot of people thought," admits a senior House GOP aide.

Despite the hurdles, Republicans are united on cutting social programs such as welfare and Medicaid and curtailing the federal role in environmental, worker-safety, and financial regulation. But divisions are surfacing over whether

to scrap corporate benefits, such as subsidies for small business, export promotion, and agribusiness. Groups as diverse as the libertarian Cato Institute and the moderate Democratic Progressive Policy Institute have targeted tens of billions in direct company subsidies. "This is the essence of special-interest spending policy," says PPI Vice-President Robert J. Shapiro.

GRUMBLING EXECS. Such heady talk tends to spook some Republicans wary of antagonizing longtime business allies. Corporate executives love to blast big government, but many companies have become nearly as reliant on federal handouts as welfare mothers. Citizens Utilities Co. in Stamford, Conn., uses cheap, federally subsidized loans for construction of telephone, water, and gas systems in fast-growing exurbs. Last year, 6.5% of its \$751 million in long-term debt was backed by the Rural Electrification Administration and the Rural Telephone Bank. An additional \$311 million was issued as tax-free industrial-development bonds. Citizens' payoff: sharply lower borrowing costs for its subsidized debt and \$108 million in earnings for the first nine months of 1994.

Republicans are similarly divided over how much to relax regulation. While companies grumble about federal rules, they'd prefer a unified set of standards to 50 conflicting state regulations. For instance, companies with uniform health plans would hate to design new benefit plans in order to meet different rules in different states. Says Federal Express Chairman Smith: "There are all kinds of things that a large multinational employer will have to deal with differently from state to state."

Another problem: turf-conscious committee heads. Senator

OHIO

George V. Voinovich

Call him a Republican innovator. Ohio Governor Voinovich has begun one-stop shopping for family services and has applied "total quality management" techniques to improve government efficiency. The number of clerical steps required to process workers' compensation claims, for example, has dropped to 7 from 17.

No surprise that he thinks states should get more freedom to run federal programs. "People who are closest to the problems are best capable of solving them," he says. He's open to suggestions that Washington stop funding some programs—even his favorite, Head Start. But Voinovich says if Congress scales back, it must give states time to adjust.



Even at this stage, some targets have been taken off the

ck O. Hatfield (R-Ore.), who as chairman of the Appropriations Committee amasses power by doling out dollars, will be a reluctant reformer. So will House Transportation & Infrastructure Committee Chairman Bud Shuster (R-Pa.), who wants to keep distributing goodies rather than letting states decide which roads to build or repair. Says Robert W. Poole, president of the Reason Foundation, a Los Angeles-based libertarian think tank: "We're still fighting powerful interests over the status quo and members of Congress who love to eat out pork."

For every unwilling committee honcho in Washington, though, there is a governor or mayor champing the bit. For them, the battle over downsizing represents a historic opportunity to redefine the relationship between Washington and state and local governments. Already, some governors want Congress to change the Constitution to give states more power: Led by Utah's Michael Leavitt, they are pushing to convene the first national meeting of the states since the Constitutional Convention in 1787. "The federal government and the states have developed a master-servant relationship," Leavitt says. "States need to assert themselves."

Ohio officials, for instance, figure they spent \$3 million in 1994 to enforce federal rules. Recently, a dozen states have refused to comply with a new law that allows people to register to vote when they apply for driver's licenses. They insist they will continue to ignore the statute until Washington finds the money to pay for the program.

The defiance is paying off. With Clinton's signing, Congress will soon adopt legislation that will make it tougher to impose unfunded mandates on states and cities. And to provide more freedom in running federally funded programs, Clinton has waived Medicaid and welfare rules for more than a dozen states. Colorado, for instance, is encouraging welfare recipients to work by allowing them to earn more than federal rules allow. "We can do a better job and spend less money if we have flexibility," explains Governor Romer.

DOWNSIZING PATTERN. Not surprisingly, while governors want more control over programs, they worry that Washington's downsizers won't provide enough money to run them. Republicans plan to turn over poverty programs, including welfare and food assistance, to the states. But they'd limit overfunding. Such expanded burdens have officials fretting that some services will be dropped altogether. Philadelphia Mayor Rendell says he could accept an 8% cut in federal aid in exchange for more flexibility. But, he adds, "if the line is drawn at 33%, it's a disaster. Our homeless population will increase tenfold."

Already, state experiments have run into problems—adding a warning to Washington reformers who have looked at popular governors such as Massachusetts' William Weld as examples of what government can do when it sheds bureaucracy. In Massachusetts, services from Weld's privatized highway cleaning and state health programs have improved, but the state is charging highway contractors with violating wage laws and health contractors with misusing funds. Under pressure from labor unions and the Democra-

tic legislature, Weld has been forced to put his privatization efforts on hold.

Florida Governor Lawton Chiles likewise won praise for turning care of Medicaid patients over to health-maintenance organizations. But he recently froze the program's expansion after a newspaper reported that HMO owners were earning exorbitant salaries with state money while offering poor-quality care. And in Oregon, state officials concede that, even after five years, their vaunted benchmarking program has a considerable distance to go. "The more we work at this, the more we realize how tough it is," says Duncan Wyse, executive director

WISCONSIN

John O. Norquist

How should city government work? At least as well as the private sector, says Milwaukee's Democratic mayor. John Norquist studied the turnaround at hometown motorcycle maker Harley-Davidson Inc. to figure out how to make Milwaukee work

better. His most striking innovation: joining with business and nonprofit groups to develop Project New Hope, which helps

welfare mothers trade benefits for jobs.

An outspoken advocate of limited federal government, Norquist is sharply critical of federal transportation and housing policy. "Cities need to be able to sell off or manage public housing on their own," he says.



of the Oregon Progress Board, which runs the program.

Indeed, the gulf between bold downsizing talk and results remains wide—and Washington has yet to initiate seriously tough action. Many companies in financial trouble bravely resolve to restructure, but they find it difficult to follow through. The same may be doubly true for Beltway politicians. GSA's Johnson says: "I'm not at all sure that the federal government is capable of making those kinds of changes from within."

Already, some programs have been taken off the table in the face of pressure from powerful constituencies. Many in Washington would dump the grossly inefficient veterans' health-care system and simply give vets free care for service-related disabilities through the normal medical system. But with a powerful veterans' lobby representing million of votes, they'll never do it.

Unless politicians want to face another bloody rendezvous with an angry electorate, though, they had better start re-making government. After watching American industry retool to confront the rigors of the 21st century, voters expect no less from the purveyors of services in Washington. That's because in government, as in business, the customer may always be right.

By Howard Gleckman and Susan B. Garland in Washington, with Richard A. Melcher in Chicago, Joseph Weber in Philadelphia, and bureau reports

due to pressure from powerful constituencies

GETTING SMALLER WITH AL

How Gore sees the future for reform

The GOP's election victory has spurred a dramatic acceleration in Vice-President Al Gore's "Reinventing Government" program. On Jan. 6, Gore met with Washington Bureau Chief Lee Walczak and White House correspondent Susan B. Garland and discussed the Administration's plans for reengineering the federal bureaucracy.

Q: House Speaker Newt Gingrich says U.S. corporations have had to restructure, and it's time for the government to follow suit. Do you agree?

A: We've been doing it for two years. He wants me to talk to Republicans about how best to do it, and I look forward to that. In the past—including 12 years of Republican Administrations—there was lots of talk about reducing the size of government, but it increased. This is the first Administration that has actually cut the size of government.

Q: Do you think people know that?

A: It's not a story that has gotten widespread coverage. I read previous reform studies and organized my Reinventing Government (REGO) effort differently—from the bottom up, by talking to employees. I didn't just stumble upon that approach. That came from consultations with CEOs and heads of public-sector organizations.

Q: Republicans want to kill five Cabinet agencies. You still seem to be tinkering at the edges. Can't you find one department to eliminate?

A: Cabinet departments don't get created by accident. Below that level, there are many agencies that we have eliminated. In one year, we downsized by 100,000 employees. We have locked in place plans to eliminate another 200,000 workers. That's a bold start.

Q: Can you honestly tell people at the grass roots that we need an Energy Dept., an Interior Dept., a veterans department, and a Cabinet-level Environmental Protection Agency?

A: People at the grass roots are also asking: "Why can't we have clean water coming out of the tap?" That's why the EPA was created. But I don't know the answer to your question yet. I do know that the departments of Energy, Housing & Urban Development, and Transportation have been through the mill, and they've emerged greatly downsized. They succeeded in defining their core missions in a way that demon-

strated we're better off with them than without them.

Q: Which management principles guide your REGO efforts?

A: One, look at the business from the customer's point of view. Measure performance. Shift from red tape to results. Empower employees and give them the flexibility they need to do the job. And then, cut back to basics.

Q: What's next for the REGO drive?

A: Round Two is going to focus on whether certain government activities are necessary at all. Each agency and department is being confronted with a basic challenge: reinvention or elimination.

Q: Historically, Washington assumed so many powers because states couldn't protect their citizens. Can they now?

A: In some cases, yes; in some cases, no. There are functions that can be better performed by state and local governments,



“In one year, we downsized by 100,000 employees. We have locked in place plans to eliminate another 200,000 workers. That's a bold start.”

functions that 20 years ago they could not or would not have been able to perform. I recently signed an agreement with Oregon that devolves major responsibilities to that state, because it can handle them better than we can. There are also cases where we turned something over and it has not worked.

Q: For instance?

A: Oh, look at interstate pollution flows, where you don't have cleanup incentives that go across state lines to the source of the pollution.

Q: Is there merit to the GOP's call for a regulatory freeze?

A: No more than there was in the call for a [nuclear] freeze in arms control. Both are simplistic approaches.

ARE AMERICANS REALLY THAT ANGRY?

Before Gingrich & Co. start slicing away at the federal government, they should study a new BUSINESS WEEK/Harris Poll gauging the public's views on the subject. Americans aren't satisfied with the way the federal bureaucracy works, but 55% believe that it's more efficient than not. And only 44% are in favor of major restructuring—49% believe that the problems could be overcome with Clinton-style fine-tuning.



HOW WELL IS GOVERNMENT WORKING?

Regardless of whether you like specific programs or not, how efficient do you think federal agencies and departments are?

Very efficient	7%	Not efficient at all....	13%
Somewhat efficient	48%	Not sure	3%
Not very efficient	29%		

RATING OUR LEADERS ...

How would you rate each of the following on his ability to downsize and make government more efficient?

	EXCELLENT	PRETTY GOOD	ONLY FAIR	POOR	DON'T KNOW/NOT SURE
Senate Majority Leader					
Bob Dole	7%	35%	38%	15%	5%
House Speaker Newt Gingrich ..	9%	28%	34%	17%	12%
President Bill Clinton	7%	29%	37%	27%	0%
Vice-President Al Gore	5%	29%	40%	22%	4%
Independent Ross Perot	9%	24%	30%	33%	4%

AND THE GOVERNMENT ITSELF

Which statement best reflects your feelings?

The federal government is inefficient and needs to undergo the same kind of dramatic restructuring and downsizing that is taking place in the private sector. 44%

OR

The federal government has some problems but mainly needs fine-tuning to make it more flexible, accountable, and user-friendly. 49%

OR

The federal government basically performs well. 6%

Not sure

MORE RESPONSIBILITY FOR THE STATES

Many politicians call for shifting federal programs to the states, which they say will give governors more leeway to comply with federal mandates on such issues as environmental protection and welfare. Which of the following statements best reflects your opinion of this approach?

Shifting programs to the states should be encouraged because it limits federal spending and promotes flexibility

OR

Shifting federal programs to the states should be discouraged because it imposes more burdens without providing additional funding for compliance. 14%

OR

Shifting federal programs to the states should be encouraged on a limited basis and only if additional funds are also provided..... 63%

Not sure..... 3%

Voters, however, don't have a great deal of confidence in the downsizing skills of President Clinton—or in the abilities of other top politicians for that matter. Their favored solution: 63% of those polled support transferring a number of federal duties to the states—if the money can be found to pay for them. They're not too keen on dismantling federal agencies, though. One exception, the National Endowment for the Arts—43% of those surveyed would kill the agency.

JUST WHAT SHOULD STATES DO?

Here are some specific federal functions that politicians are thinking about overhauling. For each, would you favor or oppose shifting more control and management of these programs to the states?

	FAVOR	OPPOSE	NOT SURE
Crime prevention	78%	20%	2%
Low-income housing assistance	73%	24%	3%
Highway construction and maintenance ..	71%	27%	2%
Medical care for the poor	67%	31%	2%
Welfare	65%	32%	3%
Environmental protection	63%	34%	3%
Farm subsidies.....	58%	36%	6%

SHOULDERING THE BURDEN

If control and management of each of the programs just mentioned is shifted to the states, would you favor or oppose:

	FAVOR	OPPOSE	NOT SURE
Larger and stronger state enforcement agencies.....	75%	23%	2%
Cuts in other state and local government programs	56%	38%	6%
Cuts in services transferred from the federal government to the states.....	53%	41%	6%
Increases in state and local taxes to pay for the programs	40%	58%	2%
Less strict health, safety, and environmental regulations.....	38%	61%	1%

WHAT PROGRAMS SHOULD GO?

Supporters of smaller government are proposing to eliminate some federal agencies and programs. Do you favor or oppose eliminating:

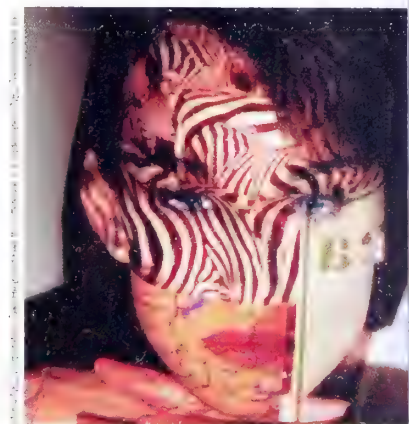
	FAVOR	OPPOSE	NOT SURE
National Endowment for the Arts	43%	52%	5%
Housing & Urban Development Dept....	38%	59%	3%
Corporation for Public Broadcasting....	35%	62%	3%
Energy Dept.	32%	64%	4%
Commerce Dept.	31%	62%	7%
Transportation Dept.	29%	67%	4%
Small Business Administration	26%	71%	3%
Veterans Affairs Dept.	22%	75%	3%

EDITED BY MICHELE GALEN

Survey of 1,249 adults conducted Jan. 4-8, 1995, for BUSINESS WEEK by Louis Harris & Associates Inc. Results should be accurate to within 2.8 percentage points.

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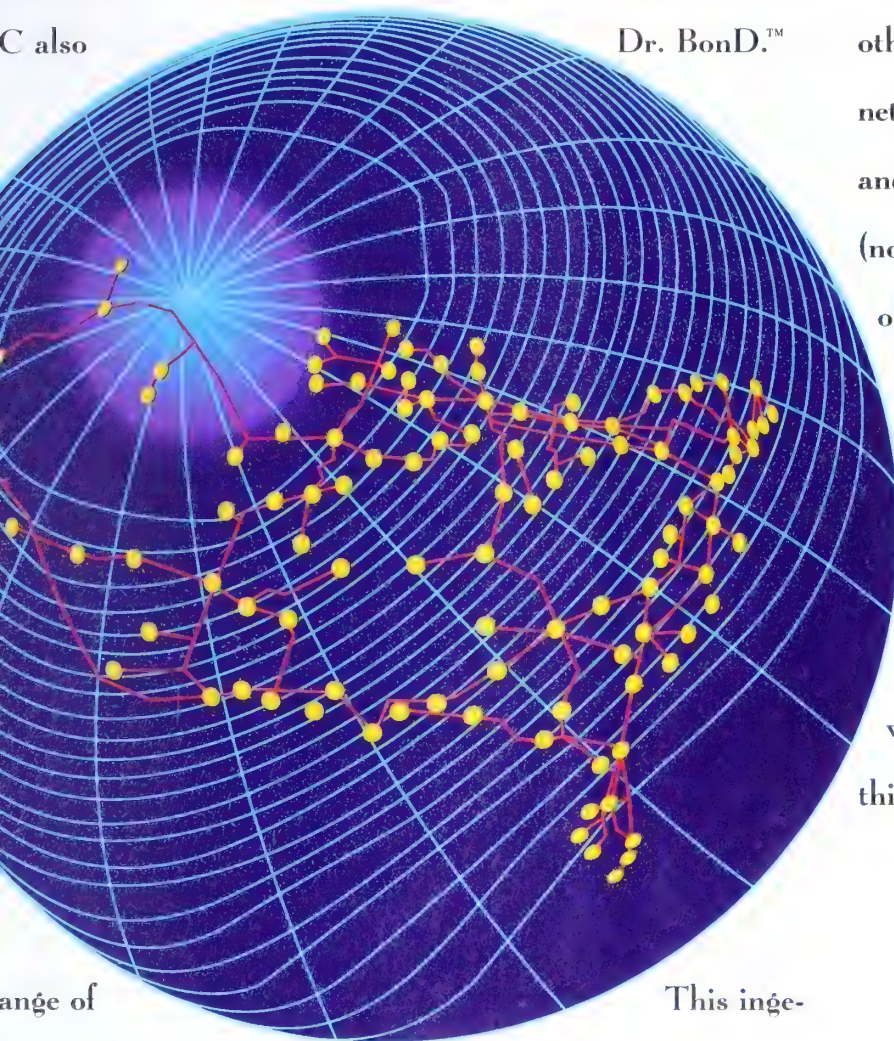
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COMPUTERS

THE APPLE OF ORACLE'S EYE

It covets Mac software as a weapon to best Bill Gates



APPLE-KNOCKER: Ellison is willing to launch a hostile takeover

It seems far-fetched, but the rumors are true: Lawrence J. Ellison, the brash chief executive of database software maker Oracle Corp., is mulling a takeover of Apple Computer Inc. As recently as Jan. 8, *BUSINESS WEEK* has learned, Oracle's board of directors discussed with Ellison his progress in assembling a plan to gain control of Apple's highly regarded operating system and applications software. A top Oracle source says Ellison is even willing to launch a hostile takeover if necessary.

Apple's stock has soared on the rumors, first published in *Information Week* on Jan. 6, though reaction from stock analysts ranges from "low odds" for success to "a bunch of B.S." Oracle insiders say Ellison is committed to besting his archrival, William H. Gates III of Microsoft Corp., in the race to gain pole position on the Information Highway. And he sees Apple's software as the key to doing that. Ellison had no



comment for the record, nor did Oracle board members. As for Apple, Chief Executive Michael H. Spindler says: "We're not shopping this company."

Meanwhile, Oracle sources say they are negotiating a partnership with Apple that would give Oracle the right to modify Apple's Macintosh operating system so that it can be used to control PCs, TVs, telephones, and other equipment on the Information Highway. Ellison wants the new system to go head-to-head with a similar product being developed by Microsoft. Apple insiders say no deal has been done yet. But an Oracle source insists it is almost ready: "We'll be ready to announce something in less than a month."

THREE-WAY PLAY? Those close to Ellison say he wants to split Apple into two companies—hardware and software—and fold the software operation into Oracle. The idea: If he's going to depend on the Macintosh operating system, he wants to try to market it more aggressively than Apple has done. Rumors have been swirling since New Year's about a three-way takeover play for Apple that would team Oracle with Japan's Matsushita Electric Industrial Co. and Europe's Philips Electronics, both major consumer-electronics companies.

Matsushita won't comment, and a Philips spokesman called the idea "nonsense." But sources close to Oracle say Ellison hopes to take only Apple's software operations, leaving its hardware to others—although the sources decline to name potential partners.

How would Ellison pay for his deal? "Everybody seems to say, hmmm, this makes some sense," says Eugene Glazer, analyst at Dean Witter Reynolds Inc.

U S WEST MAY HELP KEEP APPLE ONLINE

While Oracle Corp. lusts after Apple Computer Inc., Apple is carrying on a more modest courtship of its own.

Insiders say the computer maker is discussing a partnership with phone giant U S West Inc. aimed at boosting

Apple's lagging online computer service, eWorld. Apple, those insiders say, plans to spin off eWorld: U S West is considering a stake of 5% to 15% for an investment of up to \$50 million.

Neither Apple nor U S West will confirm the talks, but Apple has much to gain from such a marriage. The online business is growing rapidly: The \$800 million market is expected to swell to \$2.2 billion by 1997, according to Michael K. Parekh of Goldman, Sachs & Co. Apple has spent some \$100 million on eWorld, but the six-month-old service has only 50,000 sub-

scribers. Says Pieter Hartsook, publisher of a Macintosh newsletter: "Impression is, eWorld is tubing fast."

U S West has the muscle to put eWorld back on the map. It could not only cash but also distribution million customers in 14 Western states. It could quickly deliver eWorld to home and corporate phone customers **WIDE WORLD.** Apple hopes U S West will be the first of a half-dozen partners. While hoping to retain major ownership, it is discussing investment with a large media company—which could infuse eWorld with much-needed

how will they do it?" Ellison may have missed his big opportunity. Apple stock was trading in the 20s in spring, when Oracle began mulling an Apple acquisition, documents in a wrongful-termination lawsuit by a former Oracle executive suggest. On the strength of its popular new PowerPC and Macintosh computers—and acquisition rumors—Apple's stock has risen, to over \$100 on Jan. 11. That gives the computer maker a market valuation of \$5.6 billion. A hostile bid would almost certainly fetch a fat premium on top of that—perhaps a price of \$8 billion or more.

EN TALKS. Although Apple, with \$10 billion in sales, is five times Oracle's size, Oracle's own market valuation totals a rich \$13 billion. Some analysts think that gives Oracle the clout to team up with a big hardware maker that can pay for an Apple acquisition. "You'd have to look to some real deep-pocketed players, like a Matsushita, with the ability to pull it off," says Scot K. Sedla, managing director of investment research at Broadview Associates. Should Apple's stock take a big dip, analysts think an Oracle-only bid could be tenable.

Ellison may be receiving some high-profile help from the likes of junk-bond dealer Michael R. Milken. Since last August, Ellison and Milken have been discussing creation of an advanced database to be used by prostate cancer researchers for Milken's cancer foundation, CapCure. That gives Ellison the clout to solicit advice on creative financing. Milken could not be reached. Still, skepticism runs deep. If top executive and creative talent fled Apple in a hostile takeover, an Oracle victory would prove Pyrrhic. And one Oracle executive thinks Ellison may delay a bid in hopes of Apple's share price dropping. The chance. But unless Ellison makes his intentions clear, rumors likely will keep circulating that Apple is about to become a morsel—if large—takeover morsel.

*by Richard Brandt in Las Vegas and
by Rebello in San Francisco*

and with a European telecom giant. Friedman, general manager of Online Services, won't talk specifics he concedes: "How we partner with them is if we're No. 1."

critical: moving eWorld into the Apple sphere. Today, it's only for Macintosh machines. A new version is expected by mid-1995 that will run up against Microsoft's new online service. Already, analysts are predicting a Microsoft takeover. eWorld may need U.S. West to keep from being left in the dust.

Kathy Rebello in San Francisco

GOLF

CRYING FOUL ON THE FAIRWAY

Is the FTC about to break up the PGA Tour's cozy little game?

John D. Montgomery Jr. is teed off. The executive director of Rupert Murdoch's fledgling World Golf Tour wants to launch a series of international tournaments with at least \$25 million in prizes this year. But he's handicapped by the PGA Tour, whose rules limit Tour members from playing in rival tournaments. "Talk about a monopoly!" Montgomery gripes. "Everyone walks around with golden handcuffs."

The Federal Trade Commission may help Montgomery unlock those shackles. On Jan. 6, FTC staffers recommended that the agency file antitrust charges against the PGA Tour, which runs almost all U.S. pro golf events. If the commissioners approve legal action, and if the case against the PGA Tour succeeds, it "would transform the tight-knit world" of professional golf, says Marcia Chambers, a Yale Law School administrator who is writing a book about women and golf.

The focus of the FTC probe, which began in 1990, is two PGA Tour rules that allegedly impede competition, according to sources close to the investigation. One requirement bars players from entering a non-Tour event on the same day as a PGA Tour contest without the Tour's permission. The second bars Tour members from appearing on TV in a non-Tour event without Tour approval.

The PGA Tour vows to fight any FTC charges and contends its rules are the basis of golf's stunning success. In 1995, television will broadcast 1,000 hours of pro golf, up from 168 hours 10 years ago. A new cable channel devoted entirely to golf will make its debut on Jan. 17. And prize money has skyrocketed, to \$111 million in 1994 from \$21.9 million a decade earlier. The reason, Tour officials say, is that they can guarantee corporate sponsors and network and cable-TV executives that golf's stars will play in Tour events. "We have not

used the rules to constrict but to carefully incubate new television and golf projects," says PGA Tour Commissioner Timothy W. Finchem.

Some international stars, such as Australia-born Greg Norman and Spain's Jose Maria Olazabal, may be more willing than other players to challenge the Tour's restrictions. They want to shoot birdies and eagles in other, possibly more

lucrative, international tournaments. And promoters of such made-for-TV extravaganzas as the *Skins Game* would like to be freed from their relegation to the off-season months—November and December—when there are no scheduling conflicts with the Tour. Murdoch's World Golf Tour, which envisions eight international tournaments a year, including four in the U.S., may have to scale back to half a dozen events this year because of the PGA Tour's restrictions.

HEAVY PURSE. But most players, sponsors, and media execs don't want to buck a system in which they have, in fact, prospered. "There doesn't seem to be anything broken," says Michael J.

O'Malley, general marketing manager of General Motors Corp.'s Buick Motor Div., which sponsors four PGA Tour events.

Many U.S. players, indeed, aren't very excited at the prospect of dueling promoters. They're unlikely to sign with Murdoch's tour, since the PGA Tour has threatened to suspend any renegades—even though each World Golf Tour event would offer \$3 million in purses divided among 40 players, far richer than the PGA Tour average of \$1.5 million divvied up among 70. Nor are they likely to cheer the FTC's antitrust drive. "We wouldn't dream of disrupting a system that's so successful," says Robert Wrenn, a 10-year Tour veteran. Whatever the FTC thinks, America's pros seem to like their shackles. After all, they're made of gold.

By Catherine Yang in Washington



NORMAN: Willing to buck the PGA Tour's restrictions?



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The world's favourite airline



AFTERBURN: With Maurice out, BA is flying the coop

ADVERTISING

UGLIER AND UGLIER AT SAATCHI & SAATCHI

It's stung by mutiny and a vengeful new rival: Maurice Saatchi

Call it The Fall of the House of Saatchi. In December, Maurice Saatchi, chairman of advertising giant Saatchi & Saatchi Co., was ousted in a boardroom coup led by dissident American shareholders. Days later, major clients put their accounts up for review. Next, seven key executives resigned. Maurice and his brother Charles, who co-founded the firm 25 years ago, unloaded nearly two million shares of free-falling Saatchi stock. Finally, on Jan. 11, Maurice announced his revenge: With defecting executives, he plans to create a rival agency—with an in-your-face working name: The New Saatchi Agency. Pulp-fiction writers couldn't have produced a better script.

But this is no dime-store novel. The events have rocked the venerable Saatchi & Saatchi to its foundations. Now, serious doubts are being raised as to whether the world's fifth-largest ad company can survive intact. Corporate clients are threatening to defect in droves. On Jan. 11, British Airways PLC announced that it will terminate its contract with Saatchi in four months. British retailer Dixons Group PLC hinted it may follow suit. Candymaker Mars Inc. put its account up for review.

Through a spokesman, Maurice denies that he is behind the personnel and account defections. Cold comfort for Saatchi & Saatchi and its 11,000 employees, though. Since the row began, the firm's U.S. shares have dropped by one-third, to under \$5 on Jan. 11 (chart)—and they're off a staggering 98% from their peak of over \$300 in 1987, the year Maurice became chairman.

Now, Saatchi & Saatchi CEO Charles T. Scott is scrambling to raise cash to keep the agency afloat. Industry sources

say its Minnesota-based subsidiary, Campbell Mithun Esty, is being shopped around by investment bankers—with a \$60 million price tag. The rub for Scott: Breaking up the company could give the Saatchi brothers a chance to win back control of the core Saatchi & Saatchi ad business, which accounts for half of the holding company's \$1.2 billion in reve-

nues, leaving other units for another buyer. "I don't think they've ever given up the idea of getting back their company, and I believe future events will bear that out," says Roy Warman, an ex-Saatchi executive.

How did the agency come to such a pass? Back in the booming 1980s, it was

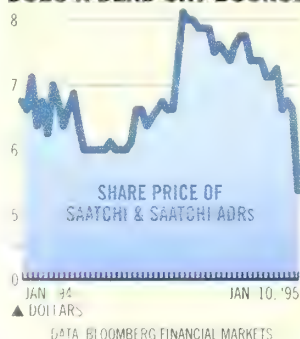
an open secret that the Saatchi brothers were far from disciplined managers. But their empire only began to unravel in 1990, after a wild expansion spree produced \$1 billion in debt. Then came a deep ad slump. Almost bankrupt, the brothers were forced to turn the company over to fresh management, and a major restructuring resulted in the creation of new shares scooped up by American investors.

LEGAL HANDCUFFS. But some investors notably David G. Herro, now a fund manager at Chicago-based Harris Associates, have been unhappy with the shares' weak performance. In early December, Herro joined with other dissident pension and mutual funds controlling 30% of the shares and ousted Maurice as chairman, citing his vituperativeness and free-spending ways as the reason. Shareholders, however, seem to have underestimated Maurice's pull with executives and clients.

The latest executive defections make Saatchi & Saatchi's prospects dicey—even if no-compete clauses in the defectors' contracts may keep them from taking on their ex-employers until next year. Gone are co-founder Jeremy T. Sinclair, considered Saatchi's creative genius; William Muirhead, who heads the Saatchi ad network in the U.S. and leads the flagship British Airways account; and David Kershaw, chief of the London-based Saatchi agency. Other departees include key creative people and the joint heads of Saatchi & Saatchi British ad unit Moray MacLennan and Nick Hurrell.

Client defections, meanwhile, will pinch the agency's finances. Mars alone accounts for \$400 million in billings. It has invited Ogilvy & Mather Worldwide Inc. and BBDO Worldwide Inc. to make pitches for its Pedigree pet food account. Other rivals are expected to bid on Mars' candy business. Even cli-

DOES A DEAD CAT BOUNCE?



...s who say they are sticking with the
...ency are getting rattled. Says Gary
...Moss, vice-president of global adver-
...ing for Campbell Soup Co.: "This is
...y serious. We just lost the senior
...son who ran our advertising busi-
...ss. We need to talk to our country
...nagers and figure out what to do."
...What's the next plot twist? One sce-
...rio has Korean media baron W. Y.

OTOS

HOCKER AT GM: PEOPLE LIKE THE IMPACT

...e carmaker may roll out 7,500 electric cars over 18 months

...he Impact, General Motors Corp.'s
...on-again, off-again electric car,
...seems to be on again. Two years
...e, GM brass pulled the plug on pro-
...tion of the zippy two-seater, saying
...was a surefire money-loser. Today,
...ough, the carmaker is quietly pre-
...ing to build as many as 7,500 Im-
...acts during the next 18 months—with
...first models due as soon as year-
...l, say former GM executives and oth-
...industry officials familiar with GM's
...ns.

...The Impact's probable resurrection
...strates a big change in the auto
...business: The movement to build
...races cars is shifting into
...h gear. Until now, auto
...manufacturers have vigor-
...ly fought tough new
...environmental laws, such as
...ifornia's standards for
...tually pollution-free cars.

...their gripe: Consumers won't want to
...y the extra cost the technology will
...quire. But GM's quiet preparations to
...ld the Impact come just as Honda
...tor Co. has announced a superclean
...sion of a conventional gasoline en-
...e that meets some of California's
...ghest strictures. Now, rivals may
...ve to move ahead fast, too, or risk
...ng left in the dust.

ADLINE DERBY. Both of these new
...velopments could undermine Detroit's
...ims that it can't meet California's
...gh emissions standards. Engineers
...many of Honda's competitors have
...g said a clean-running car, known
...an Ultra Low Emitting Vehicle
...LEV), would have to burn an alterna-
...e fuel such as natural gas, and would
...t about \$2,000 more than gasoline
...sions. Carmakers may have to start
...ling ULEVs in California as early as
...7, while Zero Emission Vehicles,
...hich currently means electrics, will
...required starting in 1998. With its

Choi, advised by former Saatchi exec
Richard Humphreys, buying the Bates
Worldwide advertising network Saatchi
acquired in 1986. That would leave
SSAW free for the Saatchi brothers to buy
or raid. Choi offered \$400 million for
Bates in December, but was rejected.
"Bates is not for sale," says Wendy
Smyth, Saatchi & Saatchi's CFO.

And Herro? Despite the bedlam he

helped unleash, he remains unrepentant.
"Everyone knew Maurice would do
anything and everything" in response,
Herro says. "But there was a majority of
shareholders, a unanimous board, and
many employees who felt the chairman
had to go." Maybe so. But they may rue
the day they touched off this melodrama.

*By Paula Dwyer in London and
Richard A. Melcher in Chicago*

for an afternoon near Disneyland.

GM officials are cagey about their
plans for producing the Impact. "We
have not made a final decision on pro-
duction," says Robert Purcell, the car's
program manager. But, he adds, "we
are very serious about making a busi-
ness out of this technology." People
familiar with GM's deliberations say it is
being spurred on in part by the fear
that upstart competitors could beat it
to the punch. The GM team was star-
tled by the variety of prototypes dis-
played at an electric-vehicle symposium
in Anaheim, Calif., in December. Some,
such as the \$16,000 convertible Tropica,
built by Renaissance Cars Inc. in Palm
Bay, Fla., are already in production.

GRAVE CHALLENGE. Current plans call
for an initial run of about 2,500 Im-
pacts, say people familiar with the
program. If the initial cars sell well,
the company could approve two more
modules of 2,500, for a total of 7,500
vehicles. To keep costs
down, GM may farm out
assembly chores to
a company that special-
izes in producing niche
vehicles.

Still, even if the auto mak-
er sells thousands of Impacts
at premium prices, the company prob-
ably won't make any money. GM spent
in excess of \$250 million developing
the vehicle, including an all-new AC
electric drive train and such weight-
saving goodies as magnesium-framed
seats. "I'll be in my grave before they
recover all those [costs]," says one for-
mer GM executive.

That's why some companies aren't
jumping as aggressively into the fray.
"I have no plans to get my vehicle out
any sooner than I have to," says Bruce
M. Kopf, electric vehicle program man-
ager at Ford Motor Co. That kind of
sit-back-and-wait approach, though,
may not be an option if California's
tough new anti-pollution regulations
remain on the books. "Whoever is first
is going to have an advantage," says
Robert C. Stempel, GM's former chair-
man and now in charge of a GM joint
venture racing to make advanced elec-
tric car batteries. And the front ranks
are already starting to form.

By David Woodruff in Detroit

new engine, Honda says it can meet
the ULEV hurdle by adding just \$200 to
\$300 in new emissions hardware, such
as a beefed-up catalytic converter, to a
conventional engine.

The Impact's price tag will be far
more—perhaps as much as \$40,000 for
early versions. But GM decided to go
ahead with the car, sources say, be-
cause consumers in three cities who
test-drove Impact prototypes last year
were entranced with it. Some offered
to pony up
nearly



Even if GM sells
thousands of Impacts,
it probably won't make
any money soon

double the \$25,000 maximum price GM
had expected to get based on prior
market research. "The biggest prob-
lem we've had is getting people to give
back the car," says Kenneth R. Baker,
vice-president of GM's Research and
Development Center.

General Motors is especially encour-
aged by how much the speedy, silent-
running car appeals to the wealthy,
its target market. "I loved it. I'd buy
one at a premium price," says Michael
D. Eisner, chairman of Walt Disney
Co., who in early 1994 drove an Impact

BANKRUPTCIES

SUSAN POWTER'S WALLET GETS A NASTY WORKOUT

As legal bills mount, can the fitness guru stop the insolvency?

This year was supposed to be another blockbuster for Susan J. Powter, the fitness guru with the bleached-blonde crewcut who has made millions from her *Stop the Insanity!* video program and books. But so far, 1995 looks like a dud: On Jan. 3, days before her third book was scheduled for release, Powter filed for personal bankruptcy in Los Angeles.

The filing comes after a three-month legal battle between Powter and her two partners. Powter blames the bankruptcy—listing liabilities of more than \$3.2 million and assets of \$500,000 to \$999,000—on the feud. “I can’t pay my bills because of the excessive litigation,” she says. “The Susan Powter Corp. made a hell of a lot of money last

and Richard Frankel, both Dallas businessmen, own the other half. Powter, 37, earns a salary based on profits but says she has no access to the revenue. “Jerry Frankel has chosen to unilaterally take control of the Susan Powter Corp.,” she says, calling her contract the “equivalent of slave labor.”

The Frankels deny they have taken advantage of Powter. Gerald Frankel says Powter gets 42.5% of net profits, while the brothers split another 42.5%, and Elizabeth “Rusty” Robertson, Powter’s personal manager, gets 15%. In the past two years, Powter has received a payout of \$3.4 million and Robertson \$1.3 mil-

claims that in 1991 the Frankels forced her to sign an employment contract she didn’t properly understand. Gerald Frankel denies the charges.

The question: How long can Powter fight the Frankels? “Susan is being sued with her own money,” says Robertson. “There’s no way she can afford to continue to do this.” According to the bankruptcy petition, legal fees so far total \$1.7 million. Robertson expects an additional \$1.5 million worth this year. **DEJA VU.** Gerald Frankel doesn’t understand Powter’s griping. If it weren’t for him and his brother, he says, Powter might still be teaching exercise classes at the Dallas fitness center she started in 1989. “We discovered her,” he says. “We invested close to \$1 million in her the first two years before we saw any profits. Before we met her, she made something like \$14,000 a year.”

But this isn’t the first time one of Gerald Frankel’s deals has gone sour. He also owns Jerrell Inc., a \$60 million Dallas-based women’s apparel manufacturer, whose retail customers include J. C. Penney Co. and Dillard Department

POWTER: “NO CONTROL” OVER THE MONEY

Stores Inc. Six years ago, Frankel got into a legal scuffle with designer Sandra Garratt, creator of the popular Units and Multiples women’s casual lines. In March, 1989, Garratt sued Jerrell for allegedly violating a licensing agreement, claiming Jerrell failed to pay her more than \$4 million in royalties and developed and marketed rival clothing based on her designs. Frankel denies the charges.

Battling Jerrell, Garratt drained her funds and filed for bankruptcy. Her suit was rolled into the bankruptcy case, and

Jerrell won exclusive rights to the Multiples line. “What’s going on with Susan sounds a lot like what happened to me,” says Garratt. “I would warn anybody if this man [Gerald Frankel] comes anywhere near you, run away screaming.” For Powter, who rose to fame exhorting women to “Stop The Insanity!” of dieting and take control of their lives, the legal insanity may just be starting.

*By Stephanie Anderson
Forest in Dallas*

THE POWTER MACHINE

TELEVISION *The Susan Powter Show*, a syndicated daily women’s issues talkfest, debuted last September. It’s carried by nearly 200 television stations.

BOOKS Powter earned a \$600,000 advance for *Stop the Insanity!*, a best-selling book published in September, 1993, by Simon & Schuster. Powter then got a \$2 million advance for *Pocket Powter*, a paperback distillation of her diet and exercise advice. A third book, *Food*, was due for release Jan. 12.

INFOMERCIALS Two 30-minute *Stop the Insanity!* TV infomercials featuring Powter’s diet bring in nearly \$1 million a week.

VIDEOS *Lean, Strong, and Healthy With Susan Powter* is one of the country’s top-selling exercise videos. It’s one of four that Powter has produced under a contract with A*Vision, a unit of Atlantic Recording.

DATA RPR & ASSOCIATES BUSINESS WEEK

year, but it went to the company, not to me. I have no control over where all the money I make goes.”

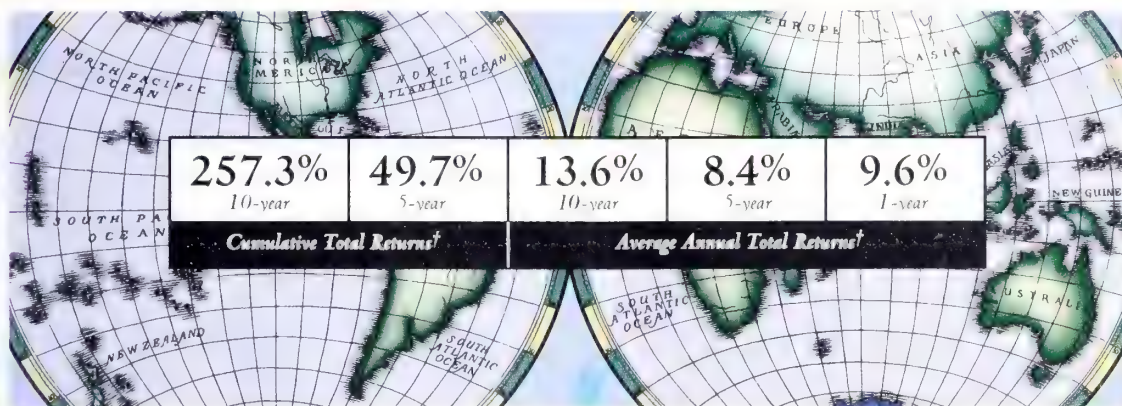
And that’s a lot of cash. What little financial information the private company divulges indicates 1994 revenues were north of \$50 million. Every cent from Powter’s ventures—including a TV show, infomercials, books, exercise videos, and clothing—goes to the company. “The question is, where is that money and was it managed properly?” says Powter, who owns 50% of Susan Powter Corp. Her partners, brothers Gerald

and Richard Frankel, both Dallas businessmen, own the other half. Powter, 37, earns a salary based on profits but says she has no access to the revenue.

The wrangling dates back to October, when the Frankels and Susan Powter Corp. sued Powter in a Texas court for breach of contract. Among other allegations, they claimed she improperly agreed to make exercise videos for an arm of Atlantic Recording Corp. Powter, who denies the allegations, two days later sued the Frankels and the company in Los Angeles Superior Court for fraud, deceit, and breach of contract, among other charges. She



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EDITED BY KEITH H. HAMMONDS

THE FAA PLOTS A NEW FLIGHT PLAN

A SLEW OF PLANE CRASHES appears to have lit a fire under the lumbering federal air-safety bureaucracy. On Jan. 10, Transportation Secretary Federico Peña promised that, within 30 days, the Federal Aviation Administration will issue a plan for adopting new airline safety measures. Some of the 70 proposals—among them, improved training for pilots and maintenance crews, more anticollision radar systems, and “controlled naps” for pilots—have languished for years. But plane accidents claimed 264 lives in 1994, a big jump from 1993, under-

mining passenger confidence and giving Peña good reason to act.

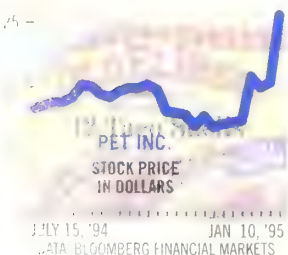
DREYFUS GETS A MR. FIXIT

CULTURE CLASH, FALLING market share, executive defections: The five-month-old union of Mellon Bank and Dreyfus has been rough going. On Jan. 10, Mellon found someone to help right its acquisition. It named retired Prudential Reinsurance Chairman Robert Riley as Dreyfus' president, replacing Joseph DiMartino, who left in December. Although a Mellon spokeswoman denies it, a source close to Dreyfus says Mellon Vice-Chairman Keith Smith had been in line for the job. But Chairman Frank Cahouet chose the outsider with fund experience instead.

CLOSING BELL

BURRITO BINGE

The Doughboy is carbo-loading. Grand Metropolitan's Pillsbury unit agreed on Jan. 9 to pay a steep \$2.6 billion, for Pet Inc.'s collection of brands, including Old El Paso Mexican foods and Progresso soups. Pet shares soared 27%, to \$25.50, on the news. Though GrandMet is paying 10% more than Pet's anticipated acquisition price, it could come out ahead, says Timothy S. Ramey of C.J. Lawrence/Deutsche Bank Securities. Pillsbury has the distribution network and war chest needed to keep Pet brands competitive, and GrandMet could sell Pet businesses that don't fit.



BORLAND'S CEO BOWS OUT

EVERYONE SAW IT COMING: ON Jan. 11, Philippe Kahn resigned as president and CEO of software maker Borland International, remaining only as chairman. That capped three years of late products, shrinking margins, and management turnover. Shareholders watched Borland's stock drop 90% in that time. Now, analysts say, Kahn's resignation may be aimed at luring acquirers. Suitors, though, likely will wait until a copyright-infringement suit filed against Borland by Lotus Development is resolved—possibly within days. In any case, says Furman Selz analyst Terence Quinn, the move may be “too little, too late.”

END OF A STANDOFF

PRO HOCKEY'S LOCKOUT IS over—just in time. On Jan. 11, the National Hockey

HEADLINER

A BLOWOUT FOR THE RUBBER WORKERS?

United Rubber Workers President Kenneth Coss may be staring defeat in the face. In July, he led 4,000 United Rubber Workers to a strike of Bridgestone/Firestone, the Japanese-owned tiremaker. It now looks doubtful that the 59-year-old unionist can avoid a major thrashing.



Bridgestone is using its worldwide facilities to keep up supply, and in early January it hired 2,300 permanent replacements. Now, even union members who return to work unconditionally, as members of the small Akron (Ohio) local attempted on Jan. 10, won't

all get their jobs back.

Bridgestone has never backed off its demand for major operating changes at U.S. factories to boost competitiveness.

The company has mandated 12-hour shifts, co-payments for health benefits, and numerous other changes. Coss is furious.

Bridgestone tactics are “an attempt to humble [workers],” he says. The U.S. isn't pleased, either. On Jan. 11, Ambassador to Japan Walter Mondale told Japanese officials that the company's Japanese CEO should talk to Labor Secretary Robert Reich.

By Zachary Schiller

League Players Association Negotiating Committee recommended a final offer from owners. That will allow a shortened season—and keep some arena owners, antsy about empty houses, from booking other acts, sources say. Eventually, the NHL will have to review costly arena leases that strap struggling owners. One possible solution: closer ties to pro basketball, whose teams are buying arenas and need co-tenants.

J&J: RED-FACED OVER AN ACNE CREAM

JOHNSON & JOHNSON FINALLY acknowledged that its paper shredder was working overtime in 1991. On Jan. 11, it pleaded guilty to obstructing justice and agreed to pay \$7.5 million in fines and costs, admitting that its Ortho Pharmaceutical unit tried to block a probe of its marketing of the acne medicine Retin-A.

The Justice Dept. charged that eight staffers shredded thousands of documents subpoenaed by a grand jury. Three executives were “separated” from the company; one, dermatology chief Lester Riley Jr., faces indictment for conspiring to defraud the Food & Drug Administration. Riley, through his lawyer, says he is “absolutely innocent.” J&J won't be charged in connection with Retin-A marketing, but the probe into individuals' actions continues.

ET CETERA...

- KKR named a new chief for Borden: Robert Kidder, former CEO of Duracell.
- Litton Industries' \$1.2 billion patent judgment against Honeywell was overturned.
- Ex-Merck Chief Roy Vagelos will join tiny biotech outfit Regeneron as chairman.
- Wal-Mart didn't break the law in underpricing smaller rivals, a court ruled.

EDITED BY OWEN ULLMANN

THE WHITE HOUSE'S NEW ECONOMIC POLICY: REELECT BILL

Bill Clinton spent his first two years in office heeding his economic advisers more than his populist instincts. He ditched his middle-class tax cut and scaled back his costly "build America" investment package in favor of a \$433 billion deficit-reduction plan. He pushed two free-trade pacts through Congress, cut the human rights tether on U.S.-China trade, and let the Fed hike interest rates six times.

But voters gave him no credit for the strong economy on Election Day. So Clinton is going with his gut: He's enlisting his economic team in a political crusade to rescue his faltering presidency—even if it means backing dubious economic policies.

That explains why an econo-squad commanded by newly confirmed Treasury Secretary Robert E. Rubin is embracing middle-class tax cuts and an 18% boost in the minimum wage—two ideas most of the team opposed in the past. Economic advisers have signed off on Clinton's "Middle-Class Bill of Rights," with its list of new entitlements. And they're mounting a statistical offensive to portray Republicans as fiscally irresponsible.

SESSIONS. Before the GOP took control of Congress, Clinton's economists felt they had distance themselves from such policy prescriptions as the nightmarish Clinton health-care plan. But the President won't tolerate independence now. Admits one official: "We used to look at things in terms of 'Does it promote growth?' But now we include political questions such as 'Does it show the difference between where the President and the Republicans stand?'"

Clinton aims to paint Republicans as wealthy elitists and Democrats as defenders of the common man. Ex-Wall Street Peter Rubin had persuaded the President to scrap the class warfare—before Clinton's job became imperiled. Now, as part of his "I'm-one-of-you" theme, Clinton is likely to propose a 75¢ hike in the \$4.25-an-hour minimum wage. He

may also jawbone companies to spend more on worker training. Both issues are obsessions of Labor Secretary Robert B. Reich. "If industry wants to continue to have a business-friendly electorate, it's got to recognize its responsibility to train its workers and raise their wages," he says.

For the past two years, the economic team largely ignored Reich—or squelched him, as when he called for cutting \$200 billion in "corporate welfare" subsidies. But now his colleagues are jumping on the minimum-wage bandwagon despite fears that the scheme might be inflationary. In reality, the Clintonites know there's little chance of getting a mini-

num-wage hike past the GOP Congress. They're mainly out to make Republicans look heartless.

COSTLY VALENTINE. The Treasury Dept. has also eagerly gone on the offensive, denouncing the flat-tax proposal of House Majority Leader Richard K. Armey (R-Tex.) as an expensive valentine to the wealthy. Meanwhile, the Treasury has produced estimates alleging that House GOP budget plans would balloon the deficit by \$725 billion over 10 years.

For the record, Clinton's econo-team insists its policy shifts are the result of a vibrant economy—not political expediency. "We have a much sounder deficit path and a robust expansion, so let's reconsider the minimum wage and the middle-class tax cut," says Council of Economic Advisers Chair Laura D'Andrea Tyson.

But that kind of reasoning only emphasizes the fact that a Clinton economic crew noted for its independence and pro-market bent has been drafted into the campaign to secure the President's reelection. All White House economic teams become politicized sooner or later. In this case, because of the GOP rout, it's sooner. And this time, the Commander-in-Chief is giving the marching orders.

By Paul Magnusson and Mike McNamee



RUBIN: Pushing a middle-class tax cut

CAPITAL WRAPUP

HUNGRY FOR PORK

House Republican freshmen talk a good game about slashing spending, but early jockeying for committee assignments belies their intentions. The most popular panel is the surface transportation subcommittee, which distributes highway funds. So many new GOPers demanded seats on the panel that leadership increased membership from 28 to 37. But Thomas E. Petri (R-Wis.), subcommittee chairman, warns would-be porkers that they'll bring home a leaner brand of bacon this year.

IS NEWT OFF-LINE?

Government scientists gripe that House Speaker Newt Gingrich isn't so technology-friendly after all. The scientists complain that House GOP budget-cutters are targeting the very research that helped create the Internet—the foundation of the Speaker's Information Highway vision. Nor does it help that Gingrich is claiming credit for getting the House and Senate online when the groundwork was laid by the science agencies and spurred by then-Senator Al Gore.

IMMIGRATION BIDDING WAR?

The White House is taking a harder line toward immigration to get ahead of congressional Republicans on this hot-button issue. Clintonites had been focusing on curbing illegal entrants, but officials also may propose reducing the number of legal immigrants. Under consideration: Cutting the number of foreigners businesses can sponsor as employees and the number of entrants from countries with relatively few emigrants, such as Ireland and other Western European nations.

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After the crash in emerging-market bourses, a search for rock-solid fundamentals

Looking tanned and relaxed despite the chaos enveloping Latin American securities markets, Argentine Economy & Public Works Minister Domingo Cavallo strode to the podium in a CS First Boston conference room in New York on Jan. 11 and declared flatly that under no circumstances would he ever allow his country's currency to follow the fate of the Mexican peso. "De-value?" he asked a questioner with a shrug. "No way."

If only investors around the globe were willing to take Cavallo at his word. Spooked by the 38% plunge in the value of Mexico's currency since December (page 58), traders have been circling emerging stock, bond, and foreign exchange markets across Latin America and as far afield as Eastern Europe and Asia, trying to get out before another developing country loses its way.

PANIC SELLING. Then came Jan. 10—"Black Tuesday" in the eyes of many emerging-market investors. As domestic interest rates soared close to 50%, and an auction of hard-currency-denominated government debt drew practically no bidders, Mexico's already weakened stock market plummeted 6.3%. In Argentina (page 32), stocks dropped 9.6%. Chile's market tumbled 4.9%. And it wasn't just U.S. and other international investors who were taking their money home. In many markets, panicked local pension-fund managers and individuals were selling indiscriminately. "I'm concerned about the crash in Mexico and Latin America," hedge fund manager George Soros told a Bucharest audience the day after.

"That, I think, can have very severe repercussions throughout the world."

One effect may be to lure more money back to the U.S., where growth and profits remain strong. "I see tremendous values right here," says Joseph Rosenberg, who manages some \$25 billion as chief investment officer for Loews Corp. "Why would I want to run over there?"

Amid this competition for capital, the Mexican crisis is forcing a wholesale re-ordering of the emerging-market scene. Burned by the shock devaluation in Mexico and enticed by increasingly tempting interest rates in the U.S.,

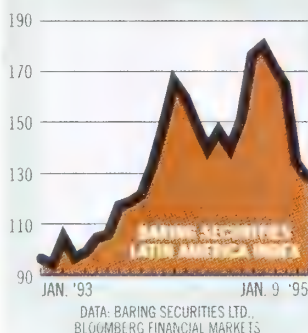
Canada, Europe, and Australia, investors are suddenly becoming a lot more choosy about committing their cash to the hot developing economy of the moment (page 102).

As high global interest rates deflate the emerging-market bubble of the early 1990s, investors are finally beginning to demand hard evidence of solid economic expansion, rising domestic savings,

steely-eyed fiscal probity, and a measure of political stability. On top of that, investors want to see economies that can garner large amounts of direct industrial investment and thus won't be held hostage to the vagaries of short-term capital flows. Says Grace Pineda, manager of the Merrill Lynch Latin America Fund: "This is a warning sign about choosing your countries and demanding more in the way of economic fundamentals."

Over the long haul, this new pickiness may have the effect of putting more countries on the path toward the eco-

LATIN STOCKS TAKE A DIVE



nomics straight and narrow. But in the short run, it's also likely to mean considerable pain for Mexico and other countries whose economies can't stand up to tough scrutiny—or who have political leaders unable to market their countries' attributes around the world.

After the current and former Mexican Finance Ministers failed to gain the confidence of Wall Streeters in two separate

Some money managers want nothing to do with Lat

earances, for example, Argentina's Cavallo jetted to New York to hold investors' hands. "Our system is robust, our policy is right," he insisted, noting that countries that depreciate their currencies will surely face inflation, unemployment, and stagnation. "Devaluation is never the solution," he added. "If you think that's not the case, look at Mexico."

RISK OF RISK. Will investors buy this time? Many economists think Argentina will force high interest rates and a sharp slowdown upon itself to defend its currency and reputation. In fact, as Cavallo tries to set Argentina apart, the tiering of emerging markets is al-

ready at a high level of domestic savings and capital controls that keep hot money from overwhelming its markets. And Argentina, notes Cavallo, needs very little portfolio investment to carry on. It plans to sell \$3 billion worth of export-oriented power and chemical plants to overseas producers this year. And, compared with Mexico, which wants international credits to help reassure investors holding some \$17 billion in government debt sold abroad, Argentina is only planning to raise \$900 million in securities markets overseas in 1995.

Still, some money managers want nothing to do with Latin America until Mexico's mess is resolved. So they are

Kong-based chief investment officer for NatWest Investment Management, "Asia looks much more safe."

But many investors are steering clear of any emerging market at all. While most U.S. equity mutual fund investors have remained remarkably calm despite hefty drops in the prices of their shares, those who bought fixed-income funds that invested in Latin American instruments are fleeing in droves. Alliance Capital Management, for one, has been hit hard with redemptions in its \$2.3 billion North American Government Income Trust. The fund was down 30.8% in 1994 and is off another 11.5% in January. With some 50% of its assets invested in Mexican and Argentine debt, the company has seen investors pull \$230 million out. Twenty-two shareholders recently sued the fund, alleging that

its name was misleading. An Alliance spokeswoman declined to comment.

GROWTH FACTOR. But if the market mess in Mexico took investors and money managers by surprise, they may have only themselves—and their brokers—to blame. Right up to last month's peso crash, many securities houses, still looking to sustain their hugely profitable business underwriting emerging-market equity and debt, were still recommending Mexican stocks and bonds as stable, sound investments. Says Goldman, Sachs & Co.'s Latin American research chief, Jorge O. Mariscal: "There was no fundamental reason to conclude that the peso was overvalued."

Given Mexico's mounting financial and political stress, that should have been a sign of a market top, but not the sign of a market disappearing. Many developing economies will continue to attract investors for one good reason: that's where the growth is most likely to be.

Still, after the latest crash, investors will approach these markets with a lot more caution in the future. "People got blinded to the risks in emerging markets," says Arnab Banerji, chief investment officer at London's Foreign & Colonial Investment Trust. More than likely, they're not blind anymore. And they'll be demanding a higher return the next time they plunge in.

By William Glasgall, with Amey Stone, in New York, Bill Javetski in Paris and Joyce Barnathan in Hong Kong



ly beginning. Despite a trade deficit, strong growth prospects, and pressure on its currency, some Latin American experts consider that Argentina, along with Brazil and Chile, will be much better able to withstand the current stress.

Brazil, for example, boasts more than \$100 billion in foreign exchange reserves and a huge trade surplus. Chile has a

diverting funds toward South Asia, which boasts two decades of economic reforms, high savings and investment rates, and robust growth. Rising U.S. interest rates and worries about China's economic and political stability hammered many Asian markets in 1994. But some economists are looking for a rebound come spring. "In comparison with Latin America," says John Quinn, Hong

Latin America until the crisis eases, so they're turning to Asia



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MEXICO

SURVEYING THE WRECKAGE

It's worse than anyone imagined—and Washington was hit, too

Just two years ago, the Sam's Club discount warehouse in Mexico City was the worldwide chain's highest-grossing champion. But on a recent afternoon the aisles were almost deserted. The rich, scrambling to beat expected price increases, had already cleaned out the last cases of Dom Perignon champagne. And, thanks to the plunge of the peso, middle-class shoppers could no longer afford most of the imported

products. Schoolteacher Beatriz Rossette frowned at a Panasonic microwave, whose 1220 New Peso (\$214) price was the equivalent of a primary teacher's monthly wage. "Forget about these imports," she sighed. "The prices are going up even on Mexican things."

As both Mexican and U.S. officials struggle to stabilize the peso and halt the plunge in Mexican markets, Mexican businesses and consumers are coming

ROAD TO NOWHERE? *Government outlays for infrastructure will shrink*

to realize they face a very different future than the bright one they had been promised. Even if the government succeeds in stabilizing the markets soon, economists say Mexico faces months of recession, layoffs, and pain. Prices are rising—despite government-ordered restraints. And companies and banks are battenning down for tough times.

Already Mercedes-Benz and Volkswagen have announced temporary shut-downs of their Mexican car and truck plants to compensate for an expected drop in demand. "The business community is in a state of despair at the downward spiral we are experiencing," says Roberto Batres, head of Arthur D. Little consultants in Mexico City.

ALBATROSS. In Washington, officials are realizing that the \$18 billion international rescue fund put together last week may not be enough. President Clinton phoned Mexican President Ernesto Zedillo Ponce de León on Jan. 10 to offer more money—if needed. Meanwhile, foreign banks are getting queasy about doling out their \$3 billion share of the package. And an International Monetary Fund team is in Mexico City negotiating what could be an additional \$2.4 billion loan. World Bank help is also likely.

Mexico is fast becoming an albatross for the Clinton Administration. It is returning to its old status of dependence on the U.S. And it looks like Mexico is now years away from becoming the stable and growing market for U.S. goods that Clinton promised as he stumped for the North American Free Trade Agreement. Quite the contrary, with Mexican wages slashed by about 40% in dollar terms, the \$1.9 billion trade surplus the U.S. ran with Mexico last year may dry up. And the austerity moves that Zedillo outlined on Jan. 3 aim to right Mexico's \$28 billion trade deficit by turning the country into a lean and mean export platform that will threaten American jobs. Some Mexicans are even talking of invoking an "import surge" clause in NAFTA that would allow them to impose import quotas and higher tariffs to ease their trade crunch.

In Mexico, officials seem stunned by their inability to calm the markets. With the sense of futility growing, there is even talk of bringing in outsiders to set up a board to manage the peso—or of abandoning the peso altogether for the dollar. Said one usually cocksure young technocrat: "In all honesty I don't know what we can do about this mess."

One of the most disturbing problems

been the almost total absence of leadership. Since announcing his recovery plan, Zedillo has been invisible. "This is more than a crisis, it's an economic meltdown," says a foreign banker. "Where's the man in charge?"

Zedillo has been hunkered down in presidential residence. He has assumed the new Finance Minister, Guillermo Ortiz, and other officials the task of being the government's public face at home and on emergency fund-raising missions overseas. The strategy seems to have been a big mistake. While adding to market jitters, it has alarmed Zedillo's recovery plan to launch. Sensing weakness at the top, the guard of the ruling Institutional Revolutionary Party, in the person of Zedillo's Energy Minister, Ignacio Piñero, has been casting doubt on proposals to sell parts of state-run oil company Pemex and electric power plants. Meanwhile, Ortiz' team of advisers is trying to find big budget cuts without much social cost. They want to maintain such programs as free health care for the poor and basic education while trimming some infrastructure projects and postponing others, such as a new subway line for Mexico City. These cuts will slam such blue-chip companies as Cemex, as well as the construction and engineering giants, ICA and Tribasa.

GE. Indeed, Mexicans are in for a tough battle. Some economists predict a 5% drop in gross domestic product in the first six months of this year. That would mean massive layoffs and bankruptcies. The banks, which already have thousands of bad loans, will come under more pressure as businesses stop paying. Many Mexican companies seem to be slipping into a survival mode. Supermarkets and hardware stores are marking down prices on staples—despite Zedillo's assurances that prices will not rise. Some car dealers have removed vehicles from their showrooms, presumably to bring them back at a lower price. Auto-parts prices are up over 20%, and even the government seemed to be giving up when it recently announced a 15% hike in milk prices.

But above all, Mexicans' grand hopes for growth and stability are about to be dashed. Zedillo came to office hoping to extend the economic reforms of his predecessor, Carlos Salinas de Gortari, to politics and social welfare. He wanted to shake up the corrupt, antiquated system. But to ride through the coming tough times, Zedillo is going to need party support. It seems unlikely he will want to take on the old guard now. *By Geri Smith and Elisabeth Malkin in Mexico City, with Dean Foust in Washington and Stanley Reed in New York*

A TALK WITH MEXICO'S FINANCE CHIEF: 'WE HAVE A SHORT-TERM PROBLEM'

The tough job of restoring confidence in Mexico's tumultuous financial markets falls heavily on Finance Secretary Guillermo Ortiz. But on Jan. 9, he seemed calm and unworried as he talked in his penthouse office with BUSINESS WEEK's Mexico bureau chief, Geri Smith, about solving his country's problems.

DEBT ROLLOVER. We're not facing a solvency problem. Mexico can easily meet its foreign debt commitments, its domestic debt commitments—even with the increased interest payments caused by the devaluation and higher level of debt. We have a short-term problem in which we have a bunch of obligations coming due soon, and we have to find a mechanism to get the markets working again so that these short-

in that case, the problem will have corrected itself.

BUDGET CUTS. We're cutting 0.8% of current expenditures, 0.5% of investment expenditures. Current expenditures mainly reflect the real reduction in expenditures that is caused by the higher inflation we expect. We will try, obviously, to preserve existing programs, to preserve essential investment in the energy sector. We'll be postponing those investments that are not so urgent. For example, there were plans to start a new metro line. This kind of thing can be postponed until the following year.

AID FOR COMPANIES. Obviously, the banks are going to have to come up with a scheme that is attractive both for themselves and the companies, to support rescheduling of small and

medium-size firms. We don't need budgetary money to do that. We can support these kinds of programs perhaps with some limited guarantees offered by development banks. So it's consistent with the budget numbers we have.

BANK BAILOUTS. What we are doing with the Mexican banks is having Fobaproa [an FDIC-like agency run by the Central Bank] take on the subordinated debt of the commercial banks in order to help them capitalize.

This subordinated debt will not be reflected in the expansion of credit because it will be cleaning up the banks' balance sheets. We also are hoping to liberalize the foreign investment regime [to allow foreigners to buy Mexican banks].

PRIVATIZATION. We are talking about [the sale of] electricity plants. The national electricity company, Comisión Federal de Electricidad (CFE), is not going to be privatized. They're two very different things. We're not privatizing the distribution. The talk is of privatization of 9 megawatts of existing electrical generation. We are not privatizing either CFE or Pemex [the state-run oil company].



ORTIZ: Confidence will return to the markets

term obligations are financed with longer-term resources. You see, no country can amortize 20% of its domestic debt in one year. So I think that we are going through some hard times.

NEW INSTRUMENTS. We are developing with investment banks a menu of options that would be offered to investors to see whether they wanted to exchange a portion of their *tesobono* [dollar-dominated, short-term treasury bills] holdings for other papers. But I think to the extent that confidence returns to the markets, the *tesobono* itself is a good instrument. It's possible that we may, in a short period of time, see a *tesobono* market working, and

JAPAN

THEY FLY THROUGH THE AIR WITH THE GREATEST OF... KI?

In Japan, execs hope to harness the "life force" in business

Few Japanese executives come more dapper and cosmopolitan than Shochiro Irimajiri, an executive vice-president of Sega Enterprises Ltd. But unaware that a journalist was watching, he appeared to come unglued on a recent evening in a Tokyo gymnasium. It started with the 55-year-old Irimajiri bowing and reaching out to touch the extended hand of Kozo Nishino, a master of *ki*—or life force. Just before making contact, Irimajiri suddenly recoiled and screamed as if he had been zapped by a ray gun. Flying 20 meters backward, he crashed into a padded wall, fell to the floor, and started writhing and yelping. Getting to his feet, he jumped wildly up and down, and then went back to Nishino for a second jolt.

What's going on here? Buckle your seat belt: This could just be the latest chapter in the Secrets of Japanese Management. For besides Irimajiri, dozens of other Japanese executives are flocking to Nishino to strengthen their *ki*. They believe this improves health and stamina, rids them of stress, enhances self-control, and keeps them youthful. Irimajiri, who visits Nishino's Tokyo center three times a week at about \$20 per session, credits *ki* with curing a serious heart ailment several years ago.

In the nine years since Nishino went public with his concept of *ki*, he has sold a total of about 600,000 copies of nine different books. Roughly 20,000 disciples have been trained at one of his two centers. But only recently has his impact on the executive suite come to light. His other high-level devotees include executive vice-presidents at Casio Computer and Mitsubishi Electric, managing directors at Oki Electric, NEC, and Sony, and Masaki Morita, chairman of Sony Life Insurance Co. and younger brother of Sony Corp. co-founder Akio Morita.

Like Irimajiri, they almost all "fly" when receiving *ki* from Nishino. "I don't particularly want to fly, but I fly," says

engineering graduate Masaaki Morita, 67. Although to an observer the flying seems akin to magnets repelling each other, practitioners say it feels good and their *ki* gains strength from it. "I haven't aged in 10 years," boasts Kazutoyo Komatsu, 66, chairman of the Japan subsidiary of Baxter International Inc., the U.S. medical products company. He produces a 10-year-old photo to prove his point. "I think *ki* has helped me grow this company from \$70 million a year to \$600 million," he adds. "It has given me a more human touch, which is very im-



TRUST THE FORCE: Nishino sends a student flying with *ki* power

portant in cross-cultural communication."

Surprisingly, what would be scoffed at as a cult in most advanced countries is gaining credibility in Japan. Consumer-electronics giant Sony Corp. has a research team studying *ki*. One Sony managing director has convinced himself and others that touching a compact disc to inject it with *ki* improves its sound. Japan's Ministry of International Trade & Industry has formed a committee to look into practical uses of *ki* energy. Committee Chairman Shigemi Sasaki, a professor at Tokyo's University of Electro-Communications, says more than 10 companies are paying for *ki* research at his university.

Just what is *ki*? Scientists don't know. Look up the Chinese character in a dictionary and you'll find a string of translations, from "energy" to "spirit" to "soul." It is the same character as the *ki* in *aikido*, the subtlest of martial arts. And it is

what acupuncturists believe courses through the body and can be controlled by needles. Nishino, unusually youthful at 68, prefers the term "fundamental life energy." He says *ki* is what Neoplatonists referred to as "psyche," which meant "breath" in the original Greek but came to mean "animating principle of the world" to the Neoplatonists.

Certain breathing techniques are critical to strengthening one's *ki*. Nishino discovered this during an *aikido* match in 1978, even though he already knew the importance of breathing in yoga and Zen. "It suddenly came to me that the soles of our feet have consciousness and that breathing is the key to the kind of special, strange power that some people have," he says. He spent the next few years experimenting 10 hours a day with various breathing techniques.

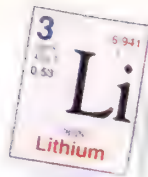
SOLE BEARING. The breathing methods Nishino espouses are relatively simple, comprising an assortment of standing,

bending, squatting, and sitting positions. Breathing is to be slow and shallow in most cases. The key, says Nishino, is to imagine that you're breathing through the soles of your feet. That "shift in consciousness" is said to positively alter the blood and oxygen flow through your body and help "awaken" each of its trillions of cells. This newly released energy is *ki*. At least, according to Nishino.

Many people do believe that breathing exercises can assist relaxation, which has widely accepted benefits. But cure a serious heart condition? Propel people helplessly through the air without even touching them? Improve product quality? It's a tough case to make.

Besides his high-profile followers and apparent results, Nishino has two things going for him. First, he doesn't behave like a modern-day messiah or even a faith healer. "He is a very normal man," says Sony Life's Morita. Second, Western science and medicine long castigated acupuncture as Oriental quackery. Then James Reston of *The New York Times* underwent an appendectomy in China in the early 1970s with acupuncture as the only anesthetic. He wrote glowingly of his experience, winning acupuncture new believability in the U.S. Maybe an equally credible Westerner someday will do the same for Nishino's school of *ki*.

By Robert Neff in Tokyo



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TALKING TOUGH TO JAPAN DIDN'T WORK. BURYING THE HATCHET WON'T EITHER

It was polite, brief, "crisp." That's how one senior White House aide described Japanese Prime Minister Tomiichi Murayama's *aisatsu*, or courtesy call, on President Clinton on Jan. 11. Talk focused on North Korean nuclear weapons, combating AIDS, and environmental cooperation. But did somebody say trade frictions? Not at this meeting.

Sadly, Murayama's visit underscores the depths to which U.S.-Japanese relations have fallen: Clinton's once-bold policy of opening Japanese markets is in disarray, and Murayama's political standing is so shaky that his weak predecessors look decisive by comparison. Tokyo bureaucrats and vested interests have stalled progress on everything from business deregulation to government reform. And with Japan's trade surplus for 1994 hitting \$62.7 billion, Clinton's trade hawks have abandoned all hope of reversing the imbalance within the next two years.

Since the collapse a year ago of the ambitious "framework" talks, U.S. Trade Representative Mickey Kantor has acceded to a slew of small market-opening agreements rather than invoking trade sanctions against the Japanese and risking disruption of financial markets.

PLAYING ALONG. Failure also weighs on Murayama. About 30 followers are on the verge of leaving his Socialist Party. That, plus his frail health, could cost his coalition control of the government within a year.

Faced with a such a political cripple, the Clintonites have decided to hold their fire. The Japanese are playing along, too. On Jan. 6, the two sides announced resumption of talks aimed at opening Japan to autos and auto parts, which comprise 60% of the trade imbalance. Significantly, no deadlines for reaching an agreement were set. And in the grand old tradition of Japanese Prime Ministers bringing "souvenirs" on trips to Washington, Japan agreed to lift restrictions on for-

eigners doing business in Japan's financial markets. But wary U.S. officials emphasize that they will closely monitor progress. They're reserving judgment on an agreement that looks suspiciously like broken promises in the past.

One reason for the cooling down of the trade fight is that both countries are looking past their festering relationship to other arenas. Commerce Undersecretary for International Trade Jeffrey E. Garten says the U.S. needs "to go beyond our decade-old obsession with Japan" and focus on cracking other Asian markets. "The battle used to be persuading people that Japan is different," worries Glen Fukushima of the

American Chamber of Commerce in Japan. "Now, it's persuading them that it matters." The Japanese, too, have diminished their focus on the U.S. and turned to investments in Southeast Asia.

But most economists think the big trade imbalance won't improve this year or next. So ignoring it is politically dangerous for Clinton. With a Presidential election approaching, Republicans will point to the one great blot on the President's otherwise successful trade policies. The next recession will probably highlight the trade imbalance as well,

as Americans lose more jobs while Japanese imports keep rising. Also, China and other Asian nations may conclude from Japan's one-sided trade with the U.S. that they, too, can run up big surpluses without fear of U.S. retribution.

With the U.S. and Japan accounting for two-fifths of the world's economy, there's no place for either power to hide the rankling issue of the trade deficit. Clinton is deluding himself if he thinks strained relations with Japan can be ignored. Both countries face a huge problem that they must resolve—soon, or not later.

By Douglas Harbrecht in Washington and Robert Neff in Tokyo



MURAYAMA: A lamer duck than ever

GLOBAL WRAPUP

SWEDISH DEBT SCARE

► Sweden's huge \$176 billion debt continues to spook the bond market. Traders drove up long-term interest rates despite the new Social Democratic government's Jan. 10 proposals to cut costly benefits. The measures, combined with tax increases, could halve Sweden's \$55 billion budget deficit over the next four years. But former conservative Prime Minister Carl Bildt calls parts of the austerity program "rubbish" because it restores some previous cuts and delays others

until 1998, while it depends on optimistic economic growth assumptions. Other critics doubt the government can muster Parliament's approval. With a lower debt rating, a boycott of government bonds by a leading Swedish insurer, and mounting pressure on the krona, Sweden is likely to be a risky investment in coming months.

WARBURG BOWS OUT

► In another blow to its aspirations to be a global player, S.G. Warburg Group, Britain's premier investment bank, is shutting down most of its Eu-

ropean bond underwriting and trading a month after a merger with Morgan Stanley & Co. collapsed. Although the \$400 billion Eurobond market was created in 1963 by Warburg's founder, Siegmund Warburg, it has become a low-margin business dominated by U.S. investment banks. Last year, Warburg lost money on bond trading. Quitting the market saves Warburg \$40 million a year but could dent its reputation as a big-league player. Rivals wonder if it will make further cuts, perhaps in its U.S. equity underwriting and distribution.

Imagine

AM I MISSING A CRUCIAL ELEMENT?

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AND THE BLOOD-RED CLOAKING?

TALKING ALPHAS? IT'S ALL SO OBVIOUS!

HOW CAN IT BE SO EASY TO MISS?

WHAT COULD POSSIBLY *happen?*





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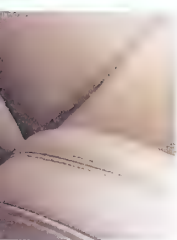


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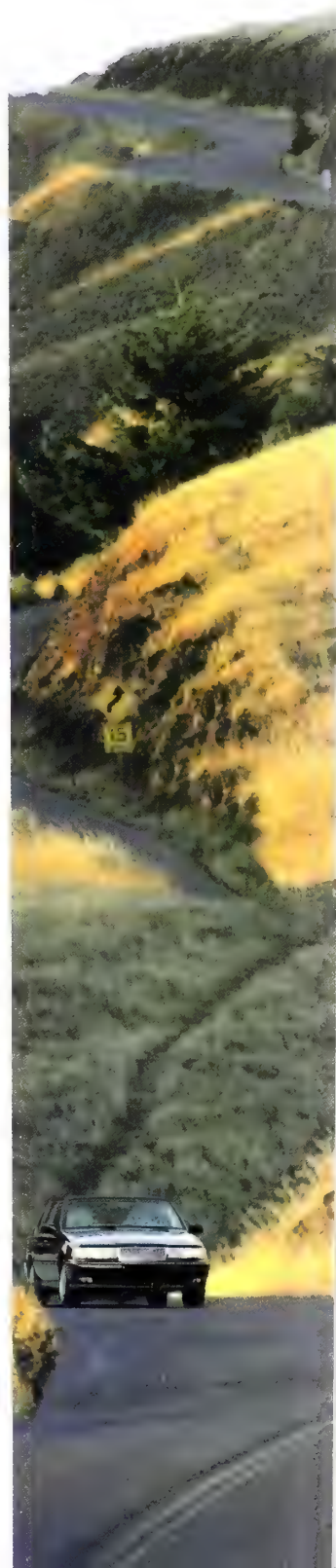
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BUG THAT MAY HELP FEED FLOSSIE WITH FEATHERS

ON C. H. SHIH, PROFESSOR of nutrition and biotechnology at North Carolina State University, can thank a dead chicken for a potentially lucrative discovery. Several years ago, while developing a process using bacteria to convert animal waste into useful products, the expired bird fell into the brew. To his surprise, it disappeared—along with the feathers, which are composed of normally indigestible protein.

Eventually, Shih found the bacterium responsible, one called *bacillus licheniformis*. The bug secretes an enzyme that can break down difficult proteins such as collagen, elastin, and keratin into amino acids. These provide an excellent, low-cost protein source for livestock feed.

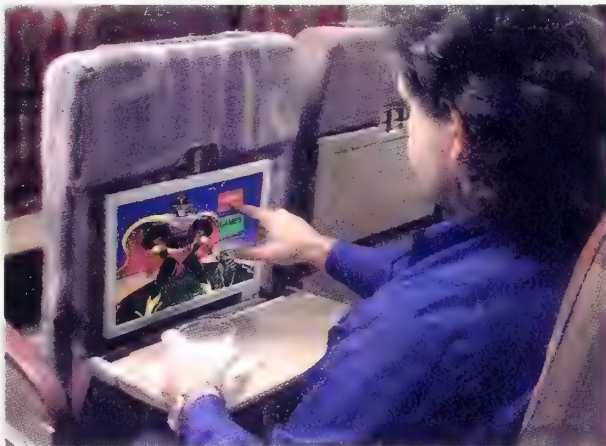
Shih estimates that the thousands of tons of feathers that are discarded each year have the potential to create a \$400 million-a-year U.S. market for feed supplements. The feather-busting bug also breaks down livestock carcasses.

The resulting amino acids could also be used as pharmaceuticals and nutritional supplements, among other uses. The university, says Shih, is currently in the process of negotiating a licensing agreement with an undiscovered company to produce the enzyme.

IN-YOUR-FACE VIDEO FUN ON AIRLINERS?

IF WIL RINER HAS HIS WAY, AIRPLANE PASSENGERS MAY be among the first travelers on the Information Superhighway. Riner, CEO of The Network Connection Inc. (TNC), is selling a digital video-on-demand system to major airlines. The Alpharetta (Ga.)-based company is known for its high-end computer servers, which manage data-flow on local-area networks. Riner has adapted the technology to deliver films and video games on aircraft. For \$300,000, TNC can equip a plane with a server, 120 seat-back displays, and a set of disk drives that store 16 hours of VHS-quality movies and games.

So far, most experiments with video-on-demand come from cable television companies, targeting thousands of users. Time Warner Inc.'s trials in Orlando, for example, deploy a video server connected to a "farm" of powerful disk drives, which zip movies to customers over coaxial cable. TNC shaved costs by working with standard PC network protocols. Each seat-back liquid crystal display is fitted with an Intel 486 microprocessor that communicates with the server. Passengers select games or movies from a menu on the LCD. The network operating system is Microsoft NT Advanced Server, and the server itself runs on a pair of Intel Corp.'s Pentium processors.



BOOSTER BUBBLES FOR ARTIFICIAL BLOOD

FOR YEARS, SCIENTISTS HAVE worked to develop substitutes for human blood. So far, though, only one has government approval—and it can transport just 25% of the oxygen that whole blood can. Now, researchers at the University of Illinois, led by chemist Kenneth S. Suslick, have a promising prospect: microbubbles of hemoglobin, the oxygen-carrying protein in blood.

These bubbles can transport 50% more oxygen than the same volume of whole blood. The microbubbles, about half the size of red blood cells, are small enough to pass through the bloodstream, but aren't likely to damage the kidneys as earlier candidates have.

The bubbles, oxygen cores surrounded by a shell of hemoglobin molecules, are created by beaming

THIS SOFTWARE IS NOT FOR FLAT-EARTHERS

MAPS ARE FLAT; THE EARTH IS not. This inconvenient fact means that measurements based on "flat earth" coordinates can be off by 10 yards or more over a distance of 100 miles. Correcting for those discrepancies is a major headache, when it's done at all. But Geodyssey Ltd. in Calgary, Alta., has developed an approach based on the true shape of the earth: an ellipsoid that bulges around the equator. Geodyssey's Hipparchus library of software tools casts a fishnet-like mesh of irregularly shaped "Voronoi cells" over the planet. Anything can be quickly located by which Voronoi cell it belongs to. The tools can handle objects ranging in size from postage stamps to hemispheres.

Hipparchus is being used by about 90 software developers, who incorporate it into programs that use geographical information. Environment Canada uses software based on Hipparchus to track icebergs; the Tsunami Warning Center in Anchorage, Alaska, uses it to pinpoint earthquakes; and Motorola Inc. is preparing to use it to position antennas for wireless-phone systems.

ultrasound waves at a water solution containing hemoglobin. The waves create tiny bursts of air into the protein solution, producing a froth of bubbles. The heat generated by the sound waves causes hot spots in the liquid, intense enough to break the chemical bonds of water. The resulting elements react with the hemoglobin to form the tiny spheres. Next step: Inject the spheres into animals to see whether they're toxic.

BIOTECHNOLOGY

BIOTECH BLOOMS IN GERMANY—AGAIN

The industry is awakening after a decade of inactivity

Late one December evening at the University of Munich, Horst Domdey and Peter Heinrich sat huddled in an office debating names for their biotech startup. BayGen or PanThera? Genex or Genetis? After three years of brainstorming and months of exhausting fund-raising, the two scientists eagerly tackled this final task. Their company—MediGene—will target gene-therapy treatments and diagnostic tools. "For 10 years, we've all talked about starting companies," says Domdey. "Now it's time to try."

So when MediGene opened for business on Jan. 2, Heinrich, 38, and Domdey, 43, joined Germany's budding homegrown biotech industry. Worried about missing out on one of the key technologies of the 21st century, Germany has reversed its practice of shunning genetic engineering and is now cautiously embracing biotech. Norbert Rau, president of biotech consultancy RauCon, estimates that the number of German companies using genetic engineering has skyrocketed from a handful to more than 100 in the past three years. Dozens more scientists are spinning off startups. Interest is so keen in the government's \$840 million in annual funding for biotech research that when it solicited 30 gene-therapy projects last year, 180 applications poured in. "Biotechnology is now a top priority," says Eckhard Lübbert, director of life sciences at the Ministry for Education, Science, Research & Technology.

The explosion of activity comes after more than a decade in which Germany sat out the biotech revolution. The risk-averse nature of its companies and banks and scarce venture capital played a role. But for

many, biotech conjured images of Nazi medical experiments, stirring opposition to biotech production. When Hoechst began building a plant in 1984 to produce human insulin, activists delayed the project for 10 years.

This convinced Bayer Hoechst, and others to flee to the U.S. and Japan to set up biotech operations during the 1980s. A 1990 law that regulated biotech helped deflect activists. But wary state officials still dragged out the approval process.

NEW RULES. Today that is changing. The law was eased last year to match that of the European Union. And now even the state government of Bavaria is helping scientists form companies. Meanwhile, Germany is lobbying the EU for even looser biotech rules. "People have calmed down," says Wolf-Dieter Schleuning, head of molecular biology at Schering. "A lot of damage was done, but biotech has a future in Germany."



HEINRICH AND DOMDEY: MEDIGENE IS ONE OF DOZENS OF STARTUPS

In fact, German researchers had already assembled an impressive track record before political opposition derailed the industry. In 1980, Germany was near the forefront of genetic engineering, holding 20% of the world's biotech patents vs. 30% for the U.S. In 1982, Peter Hans Hofschneider, now head of scientific research at the Max Planck Institute for Biochemistry, developed a method to transfer genes from one cell to another that is now commonly used. And Germany ran major clinical trials of genetically engineered drugs. Today, it holds just 12% of the patents, while the U.S. has nearly 50%.

Now, German drug giants are even looking into investing more at home. In 1993, German companies spent 75% more on biotech overseas than within their own borders. But Bayer, which is adding a \$100 million plant to its \$300 million Berkeley (Calif.) biotech operations, is so convinced that the climate is changing that it will decide this year on a bacteria-based product to be produced in Germany. "Once research comes out of the laboratory and into manufacturing, there's now a lot we can do in Germany," says Peter Stadler, head of pharmaceutical biotechnology for Bayer.

Economic forces are also fostering the new climate. In the early 1990s, cost-conscious drug giants began outsourcing more research. Moreover, many German scientists, returning from postdoctoral studies in U.S. biotech labs armed with knowledge, are eager to work in startups. "Once you found a company, people flock to you," says Domdey. Take Biopharm in Heidelberg. Many of President Michael Paulista's 25 researchers are like Science Director Jens Pohl, who returned from postdoctoral work in San Diego eager to join a small company. They started by taking on moneymaking tasks such as reviewing patent applications to sup-

HOMEGROWN BIOTECH

Biotech is taking root in Germany, aided by a less hostile public and government support.

EVOTEC Funded December, 1993, with \$7 million to commercialize technology to alter molecules developed by Nobel laureate Manfred Eigen.

BIOMEVA This R&D lab, now 75%-owned by Swiss contract research company RCC Research & Consulting, produces genetically engineered material for clinical trials by U.S. and European companies.

BIOPHARM Founded in 1986, the company isolated a bone protein, MP-52, which it licensed to Hoechst last year to develop as a treatment for osteoporosis and other bone disorders.

MEDIGENE Launched in January, 1995, with \$4 million in funding. Activities: R&D on gene therapy for non-Hodgkins lymphoma, a rapid drug screening, and diagnostic tools for heart failure.

MORPHOSIS Founded July, 1992. Has \$3.27 million in funding. Aims to develop a technology to accelerate the discovery of proteins and peptides, and a treatment for septic shock, among other projects.

DATA BUSINESS WEEK

t their research. Paulista proudly
rs the scars he inflicted while hacking
bones at a local butcher to get
ugh marrow to manipulate proteins.
ir development of a human bone pro-
is so promising that last November
echst bought the rights to develop it
an osteoporosis treatment. "I want to
w the world that Germany can do
ortant research," Paulista says.

GERMAN WAY. Foreign investors also
opportunities in German startups.
rophosis in Munich, started by two
tists in 1992 to develop new meth-
to discover and screen protein and
tides, found some 90% of its funding
side Germany. London-based venture
talist Alex Karda, who owns 33% of
stock, hopes to take it public in 1997
ugh Easdaq, a pan-European elec-
tric stock market for midsize compa-
to be launched later this year. Mor-
eis already has an alliance with Glaxo
dings PLC, which is testing peptides
discovered to treat septic shock.

German institutes are also encourag-
their scientists to think like entre-
preneurs—especially the Max Planck
society. To learn the ropes, the society
practiced in the U.S. by helping
ow scientist Axel Ullrich set up Su-
Inc. with an American partner in
wood City, Calif., in 1991. Their mis-
was to develop cancer and diabetes
gs, and the company went public
last year.

n December, 1993, MPS helped one
s directors, Nobel laureate Manfred
en, start Evotec. The Hamburg-
ed outfit will commercialize tech-
ues to speed up the evolution of
ecules to develop better drugs.

GENE THERAPY. In time, Germany may
ome a world player in biotech. Cer-
ly, its annual \$1.5 billion in biotech
pales beside the \$6 billion or so
nt in the U.S. But German drug gi-
s have joined the Swiss in snatching
American technology. Germany pos-
ses a rich network of world-class R&D
versities and institutes. Gene therapy
ains a wide-open field. And Germany
n a good position to capitalize on
e splicing, a tool that can be used to
elop chemical drugs, because it ex-
in chemistry. "It's not too late,"
s Max Planck's Hofschneider.

The U.S. is unlikely to lose its hege-
y in biotech to Germany. But as the
stry shifts to high-volume manufac-
ng, it plays to Germany's strengths
engineering and chemistry. "We will
a German way" in biotech, says
er's Stadler. Given that nation's his-
ry of industrial excellence, that's prob-
y a safe bet.

by Karen Lowry Miller in Bonn,
h Joan O'C. Hamilton in San
ncisco

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by Lipper
(10 years)

Forbes
Honor Roll
(5 years running)

18.6%
Average Annual
Total Return
(10-year period as of 9/30/94†)

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COMPUTERS

IBM: WHY THE GOOD NEWS ISN'T GOOD ENOUGH

Gerstner reshuffles staff as profits roll in from big iron—a game of diminishing returns

Louis V. Gerstner Jr. should be a happy man. By most projections, IBM is about to report stunning financial results. When the numbers come in on Jan. 23, Wall Street expects almost a 300% jump in fourth-quarter earnings—the fifth straight quarter of profits for the beleaguered computer giant. For the year, estimates Salomon Brothers Inc. analyst John Jones Jr., IBM will show a nearly \$3 billion net profit on a surprisingly strong revenue gain of 6%—to \$64.1 billion. “It’ll be the best they’ve had since 1990,” says Jones. With Jones and other bullish analysts upping estimates in anticipation of the good news, IBM shares have climbed to around 75, nearly 50% above their 52-week low.

Why, then, is Chairman Gerstner shaking

signed after being offered lesser roles in Gerstner’s new organization, which combines the worldwide sales force under international sales chief Ned C. Lautenbach and merges most software development under John M. Thompson, a senior vice-president. If anybody around IBM had become complacent, these high-profile rebukes shook them up: Both Hancock and LaBant had met their performance goals, say company insiders.

MAINFRAME WINDFALL. What prompted Gerstner’s move is the disturbing trend behind IBM’s earnings: In 1994, a huge 68% of the company’s gross profits came from high-end products such as mainframes, minicomputers, and data-storage systems, say insiders. That’s up from 65% the year before—and points IBM in a direction that will undo Gerstner’s turnaround: increased reliance on products for which demand has peaked and mar-

are locked into the big-ticket stuff.”

As it is, the mainframe surge is a windfall. In early 1994, IBM executives were projecting a 50% plunge in mainframe sales. But as the economy improved, demand jumped. Now, analysts figure mainframe revenue dipped just about 7%, to \$7 billion, from \$7.5 billion in 1993. And as part of Gerstner’s reshuffling, mainframe czar Nicholas M. Donofrio was rewarded with a promotion and control over IBM’s RS/6000 “servers” and AS/400 minicomputers as well as over mainframes.

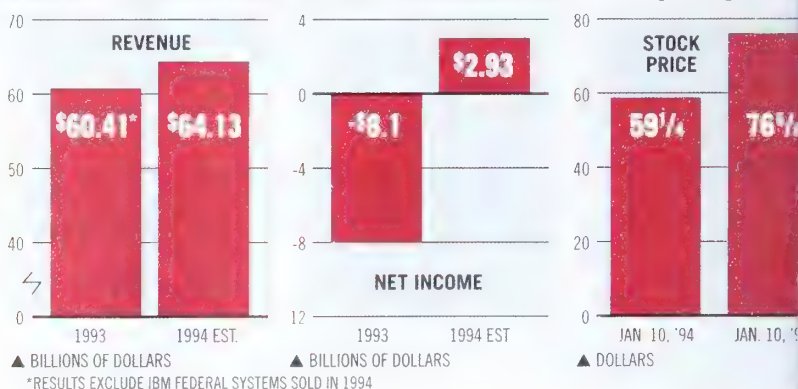
Nobody is more alarmed by the situation than Gerstner. “He’s pissed,” says one manager. “If [mainframes] weren’t holding up the company, the sheet would come off the cadaver.” Through a spokesman, Gerstner declined to discuss what he calls “plumbing” changes in the IBM organization.



GERSTNER SAYS IT'S ONLY "PLUMBING"

things up? On Jan. 9, he announced a reorganization of Big Blue’s software and sales units that immediately displaced two highly respected longtime senior vice-presidents, Ellen M. Hancock and Robert J. LaBant. Each re-

WHAT'S BEHIND THE SHAKEUP



kets are shrinking. In software, the story is the same. With \$11 billion in revenues, IBM is the world’s largest software maker; but most of that revenue is tied to mainframes. Those programs carry eye-popping 60%-to-70% margins, but growth has stalled and will fall off. “Gerstner has done a great job on the balance sheet,” says Charles Morris, consultant and co-author of *Computer Wars*. “But more than ever, they really

One obvious fix is to get the worldwide sales organization to do a better job. That’s the idea behind uniting U.S. and international sales under one executive. That way, the company can serve customers who operate across the globe without getting hung up on turf battles between IBM’s regional sales managers. “Gerstner’s had that as his desire ever since he got there,” says Gary Helmig, an analyst with the SoundView Fi-

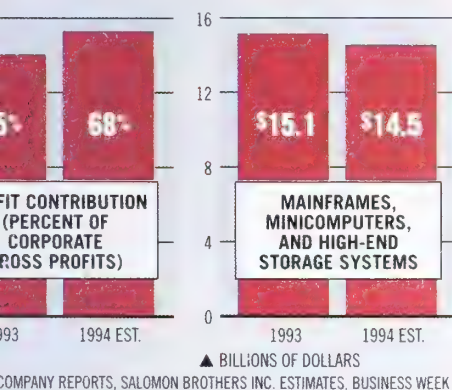
cial Group Inc. Lautenbach's internal experience won him the nod over Laut. It also helped that he had landed a big order from the government of India and signed up Hitachi, Toshiba, Canon to use the IBM-Motorola PowerPC chip.

Fixing IBM's revenue-mix problem isn't be so simple. By now, Gerstner expected IBM to be weaning itself from the profits associated with "big iron"—and making up the earnings with software sales in high-growth areas such as personal computers and software.

MARKET MISSTEPS. No such luck. 1994 ended in a washout for the IBM Personal Computer Co. It started the year with a \$700 million inventory of obsolete models, which took six months to unload. And when it came time to launch new Aptiva home PCs last fall, the company erred on the conservative side: Aptivas sold out before the fourth-quarter home-computer boom started. Says William Milton Jr., an analyst at Brown Brothers

Hardiman & Co.: "It didn't have to be that way if this company had judged the length of the consumer market adequately and had sufficient inventory." Analysts estimate that PC hardware and software operations were in the red, to the tune of as much as \$2 billion in 1994. While Gerstner is giving IBM PC Co. president G. Richard Thoman more time to straighten out the hardware business, he's taking drastic measures to repair IBM's software business. Despite

the company still gets most of its profits from product lines, where revenues are declining



investing billions in development over the past several years, IBM has yet to make serious inroads in high-growth markets for PC software, where Microsoft Corp. dominates. It also lags in client/server software, a critical technology for running corporate networks. The company, says Marc Butlein, chairman of consultant Meta Group Inc., "has demonstrated any ability to market software and doesn't understand the

mass-market nature of [PC] software."

Last spring, an internal review of IBM's software businesses concluded that most units were uncompetitive, bloated, and inefficient. No wonder. IBM has lacked a coordinated strategy. Software operations had been divided up among a number of units, which often has led to infighting and gridlock—one reason, in-



siders say, that Hancock lost a chance to head the new software unit. They say Hancock and Thompson, the executive whose appointment prompted her departure, had a long-running feud. Thompson was responsible for Personal Software Products, IBM's PC software unit. Hancock

had networking and systems software—including DB2, IBM's strategically important database package. But the two could not agree on a variety of issues, including how to manage the relationship with Lotus Development Corp., a key developer of applications for IBM's OS/2 operating system.

CLEANING HOUSE? That disagreement may have figured in IBM's internal debate over a possible acquisition of Lotus. Sources close to IBM and Lotus say that Big Blue has been among a handful of companies interested in buying the company, whose Notes program leads the market for so-called groupware. IBM sells Notes, but Hancock's group developed a competing technology. Now AT&T, which is launching Network Notes with Lotus, is regarded as a likely suitor.

Buying Lotus—a possibility IBM declines to comment on—would certainly

help. But there's lots more to do. Thompson now has a majority of the IBM software empire, including programming for PCs, PowerPC-based systems, mainframes, and networks. He's expected to come up with an overall market-

ing strategy for these products. The move follows a consolidation of IBM's software development last spring around Workplace, a core of basic software that eventually will run on everything from PCs to AS/400s.

Thompson is also expected to clean house, perhaps recruiting seasoned software talent to help IBM enter new markets. In addition to the Workplace initiative, IBM is banking heavily on object-oriented software—an approach that reuses pieces of code instead of rewriting each new

CASUALTIES
Senior Vice-Presidents Hancock and LaBant had both met their performance goals. If anyone around Big Blue was still complacent, these high-level rebukes woke them up

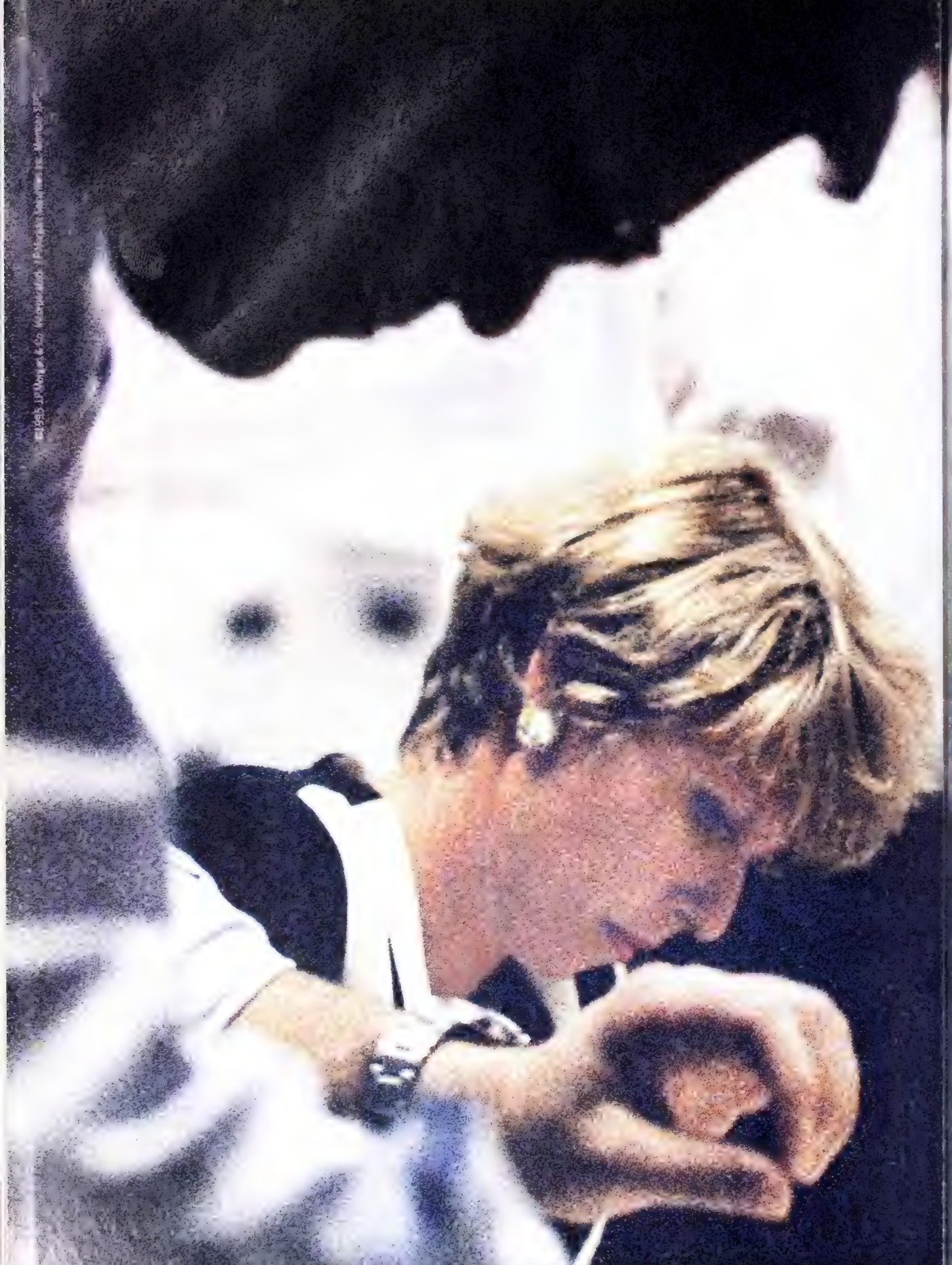


program. Gerstner has frequently cited the new software technology as a major IBM thrust.

Thompson's biggest challenge may be to finally make OS/2 a hit—or pull the plug on the 10-year effort to create a best-selling PC operating system. IBM has spent an estimated \$2 billion on OS/2—and, insiders say, will spend roughly \$1 billion this year between OS/2 Warp for PCs, which hit the market last fall, and a new version for PowerPC systems. IBM says it has shipped some 800,000 copies of Warp, but analysts estimate that the heavily discounted program has generated no more than \$25 million in revenues. Unless Thompson can turn that around—and IBM's sales army brings in revenue from new products—the era of happy earnings reports could be short-lived.

By Ira Sager and Amy Cortese in New York

LABANT: NOT ENOUGH GLOBAL EXPERIENCE



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THE COMPUTER IS IN THE MAIL (REALLY)

Once almost written off, direct marketers Gateway and Dell are thriving

Some 15 million corporate customers and ordinary consumers carted off personal computers from PC dealers or electronics stores last year. But more than a million savvy buyers chose an easier way. They simply picked up the phone, ordered the latest PC hardware, and waited for it to arrive on their doorsteps. So while the huge surge at the PC stores captured the headlines, another story was unfolding: Mail-order kingpins Dell Computer Corp. and Gateway 2000 Inc. were racking up record revenues and profits—and setting themselves on a course to dominate the mail-order channel, a 15% to 20% chunk of the \$45 billion PC business.

What makes this so surprising are all the gloomy predictions for both companies. When Apple, Compaq, and IBM said they would take to the phones to sell their PCs directly, analysts predicted that customers would flock to the big brands. Then a series of blunders made it seem that Dell and Gateway—both fast-growth companies headed by young entrepreneurs—might flame out. Stretched to its managerial limits, Dell punted in laptops and took a \$40 million charge to scrap an entire product line. It got burned on derivatives and lost a series of top managers. Last spring, Gateway's earnings plunged after a \$16.5 million inventory write-down. "You could have made the case last year that they'd go under," says Chuck Haggerty, CEO of disk drive maker Western Digital Corp. "But today, they're very, very strong and getting stronger."

"NORTH OF 60." Indeed. Gateway's revenues surged an estimated 50% in 1994, to \$2.6 billion. Its stock has jumped from 9¢ to around 22 since

last spring. Dell, whose sales for the year ending Jan. 31 will be around \$3.4 billion according to Alex. Brown & Sons Inc. analyst Steven Eskenazi, did even better on Wall Street. Its shares have zoomed from 19 last January to 46. "It could easily trade north of 60," says Eskenazi.

Why so bullish? For one thing, the mail-order threat from IBM, Compaq, and Apple has faded. IBM killed its Ambra mail-order unit last summer, and none of the big three gets significant revenue from phone selling. At the same

time, mail-order wannabes have been disappearing—folding or merging.

That leaves Gateway and Dell with 47% of the mail-order business, according to Computer Intelligence InfoCorp. Their combined share could hit 70% to 80% by 1998, says PaineWebber analyst Michael K. Kwatinetz. "A year ago everyone thought the direct market would be flat, but they're starting to see there's something more going on, and I think it's going to continue to grow faster than the PC market," says Theodore W. Waitt, Gateway's CEO.

Mail-order, in fact, now appears to have some advantages over the rest of the PC business. Rather than a schlocky backwater aimed at cheapskate PC buyers, mail-order is the preferred method for the best PC customers—experienced business clients and knowledgeable consumers looking for the most cutting-edge (and expensive) models. Dell's average customer spends \$2,700, Gateway's \$2,600, and Compaq's \$2,400. Another plus: The businesses and consumers who use mail order know what they want—and they don't need the hand-holding required by the neophytes in the stores. "We're not interested in home PCs," says CEO Michael S. Dell, dismissing today's fastest-growing segment. "We can grow at a rapid rate by focusing on our core business."

And because they build to order, rather than run up big inventories of finished systems, Dell and Gateway can be more nimble. Direct marketers whisk components into custom-configured computers as the phone calls come in, and therefore carry far less inventory—35 days for Dell, vs. 110 days for Compaq Computer Corp. For the same reason, Dell and Gateway say they



DELL CEO Michael Dell:

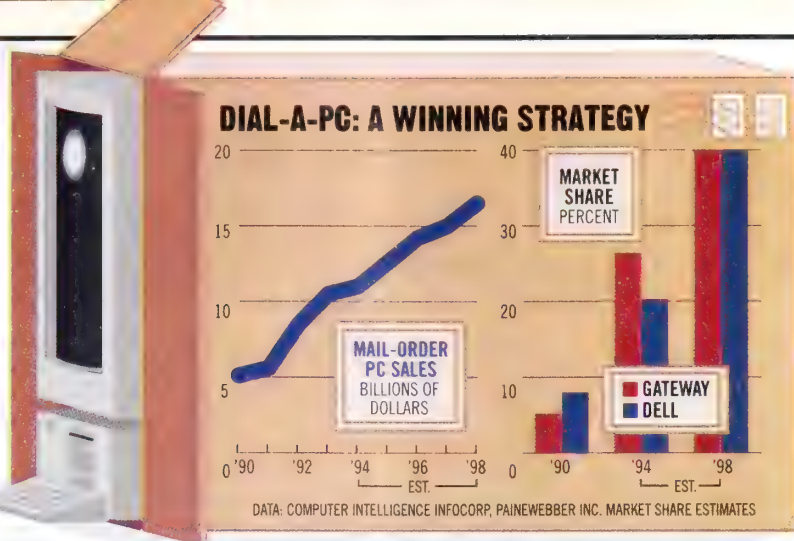
"We're not interested in home PCs. We can grow at a rapid rate by focusing on our core business."

switch to new microprocessors or disk drives much as three months earlier than PC makers go through dealers. Such flexibility is one reason why Dell and Gateway have moved quickly into the higher (and more profitable) business of selling machines based on Intel's Pentium chip. By New Year's Day, some of Gateway's PCs are Pentium-based, compared with less than 10% for

Compaq and IBM, which are selling off stocks of PCs using the older 486 chips. And Dell and Gateway are better prepared to get past the Pentium flaw mess: Having already sold their stock of PCs with the defective chips, the companies in early January were the first to announce they are using only Intel's replacement chip.

WORK NICHE. Another key advantage: Direct-mail eliminates the middleman. So Gateway's operating margins are only 5.4% of revenues, versus 13% for Compaq. And by selling direct, Gateway and Dell can afford to undercut the big brands, which need to leave a 4%-to-6% profit for dealers. "The PC makers can't sell direct without hurting the rest of their business," says Robert Anastasi, an analyst with Winston Humphrey & Co. in Atlanta.

It wasn't supposed to be so easy, as even Michael Dell attests. Afraid of leaving one-fifth of the PC market for other guys, he ordered an expensive foray into the fast-growing retail channel in 1990. It ended unceremoniously last summer when Dell pulled out of Sam's Wholesale Club and other discount chains. Now, instead of pursuing the biggest sales gains to fatten the bottom line, Dell says it's focusing on more profitable services, such as network services. Instead of aiming for 50% to 60% growth this year, it's scaling its plan to around 40%. "We're concerned about our ability to grow 50% to 60% at this size," says co-CEO Morton Topfer, a 23-year Motorola veteran brought in last year to inject some big-company experience into Dell's up-



per management. The new goal is still more than twice the expected 15% growth rate of the PC industry in 1995.

For all the good news, these companies face more complex problems as they grow. Both, for example, are wrestling with rising costs. Dell is installing an expensive internal information system and Gateway recently opened a customer-service center in Kansas City

sales. "I call us super-direct," says PC Compleat CEO Gordon B. Hoffstein. "We offer the choice of a superstore with the service of Dell."

ASIAN INVASION. Overseas expansion is one way the mail-order kings plan to stay ahead. Dell already gets 30% of its sales in Europe, but its network of country-specific outposts proved too costly. Now it has consolidated the \$800

million operation in Ireland and has pulled out of marginal markets such as Finland. It's also planning a new Asian thrust, from a factory to be built in Malaysia. Gateway, which entered Europe in 1994, is signing up distributors in Asia and Latin America.

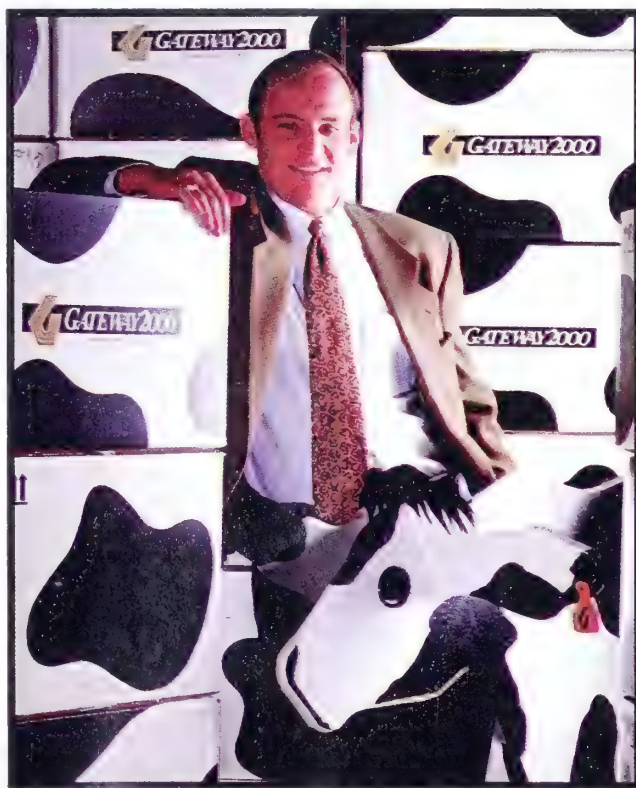
Ultimately, Dell and Gateway will only prosper as much as the direct channel lets them, and there are those who doubt it will. Digital Equipment Corp., for example, climbed to No. 3 in mail-order but is now shifting distribution to dealers. "[DEC's] PC business has reached a size where it's no longer efficient to fill orders one at a time," says Raymond L. Weadock, general manager of the company's PC unit.

Dell and Gateway aren't likely to follow suit. With consultants Bain & Co., Dell has tested new concepts such as interactive kiosks and marketing via the Internet. Meanwhile, Gateway has opened showrooms in Paris and Frankfurt to acquaint European shoppers with their wares. But both remain committed to selling directly. For now, it's hard to argue with their results.

By Peter Burrows
in Dallas

TED WAITT, CEO of Gateway:

"I think [the direct market] is going to continue to grow faster than the PC market."



COMMENTARY

By Christopher Farrell and Karen Pennar

WELFARE REFORM WON'T PATCH UP POOR FAMILIES

The numbers are staggering. In 1993, 26% of U.S. families with children were headed by the mother, up from only 12% in 1970. Among African Americans, the two-parent family suffered an even greater decline. In 1970, about 33% of black families were headed by the mother. By 1993, the number had jumped to 58%. The traditional American family structure has been disintegrating from Nob Hill to Harlem.

What accounts for the transformation of the family? Cultural changes, of course, have reduced the traditional social stigma associated with divorce and illegitimacy, while reforms in divorce laws have made it a lot easier for couples to dissolve their marriages. But politicians like to fix the blame on government and its social welfare policies. Republicans and Democrats will shortly begin to debate the merits of various plans that would sharply curtail Aid to Families with Dependent Children (AFDC), food stamps, and other benefits as a way of forcing people off the welfare rolls and into paying jobs. The objective: to restore "family values" and reduce the dependency and illegitimacy that, according to Charles Murray in his 1980 book *Losing Ground*, welfare has fostered.

NO CORRELATION. More and more, though, economists across the ideological spectrum are arguing that it's not the welfare system but powerful economic forces that are largely responsible for the breakup of the traditional American family. Murray's popular argument that generous welfare benefits have had the effect of increasing single motherhood doesn't stand up to scrutiny. For one thing, a change in benefits has only a slight impact on family structure, say economists William A. Darity Jr. of the University of North Carolina at Chapel Hill and Samuel L. Myers Jr. of the University of Minnesota. However, the

fraction of families headed by females has risen even as AFDC payments have fallen in real terms since the late 1970s. Furthermore, benefits vary widely across states—yet illegitimacy rates often don't correlate with payment levels. So, the incentives embodied in the welfare system aren't the chief cause of the decline of the conventional two-parent household among low-income families.

In reality, the weight of economic evidence points in an entirely different

are more marriageable black women than men, a result of high mortality and incarceration rates among black men. More young black men are in prison than are in college. Homicide is the leading cause of death among youths, and for black males, 1 out of 100 deaths is a homicide, compared with 1 out of 100 deaths for white males. "Black men have become less useful in the emerging economic order; they are socially unwanted, superfluous, and marginal," says Darity.



WHERE THE FAULT LIES Politicians like to fix the blame on government policies, but economists argue that free-market forces, not welfare, are largely responsible for the breakup of the traditional American family

direction: It's primarily free-market forces that have driven a wedge through families. Some of this evidence was presented at heavily attended sessions on the economics of the family and welfare during the latest American Economic Assn. annual meeting in Washington on Jan. 6-8.

A paper presented by Darity showed how declining opportunities for growing numbers of black men have made them less marriageable and led to the rise of single motherhood among blacks. There

Trends in the labor markets have played a big role. Technology and competition from low-cost foreign workers have displaced many low-wage workers and driven down the incomes of other less-skilled workers, with young black men hit harder than any other group. And the Federal Reserve Board's inflation stance has had the effect of slowing long-term economic growth. More jobs are created and more people are lifted out of poverty when growth is more robust.

not just what has happened to comes that's undermining family e. Women's wages for both and blacks have increased in rears, putting black women nearly with black men. According to T. ultz, economist at Yale Universi- women's wages rose from 73% men's wages in 1980 to 98% in r white women, the comparable are 53% and 80%.

rise in women's relative wages—outably positive development—less is having some negative ef- ury S. Becker, Nobel laureate st and BUSINESS WEEK columnist, as long ago as the 1960s that the e market is like any other mar- hich the laws of supply and de- erate. As women's job opportu- mprove and their wages rise, one or getting married is under- financial support. At the same growing number of men, espe- ack men, are less desirable mar- rtners because their earnings s are so bleak.

INCENTIVES. The overwhelming f economic forces like these sug- at lawmakers who focus solely on reform to restore traditional fam- ures will be disappointed. In- ey should extend their efforts for ways to strengthen "the bot- of the labor market," says econ- ert H. Haveman of the Univer- Wisconsin at Madison.

not an easy task, of course. onomists at the conference were roaching the prospect of a dollar ecrease in the minimum wage. 's not a widely supported op- st economists, as well as policy- worry that increasing the mini- ge could backfire by making es curtail the creation of low- os. As an alternative, a number mists, such as Haveman, favor a bsidy or a newly designed em- ax credit. Right now, private- mployers are disinclined to hire who are poorly educated, poor- ed, and already at the bottom of g queue. The aim would be to mployers an incentive to overcome uctance to hire.

won't bring back the traditional ent household any time soon. But l raise incomes and well-being— tually restore the economic of marriage.

ll and Pennar write about eco- ssues.

Media



IDIOT'S DELIGHT:
DUMBER IS A
RUNAWAY HIT
FOR NEW LINE

MOVIES

TED'S DREAM FACTORY IS RUNNING FLAT-OUT

Turner is spending \$750 million on 39 films—for starters

Dumb people are making a fortune for smart media moguls these days. First it was Tom Hanks' charming simpleton *Forrest Gump*, which has earned at least \$200 million for Sumner Redstone's Paramount Pictures Corp. Now, Jim Carrey's dim-witted antics are minting money for Ted Turner. The elastic-lipped comedian's latest film, *Dumb and Dumber*, stands to make more than \$100 million for Turner's New Line Cinema Corp.

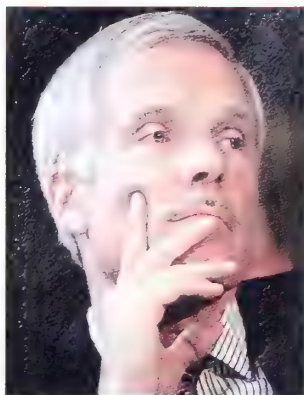
Coming from the man who invented CNN, *Dumb and Dumber's* sophomore gags and scatological jokes look awfully low-rent. But Ted Turner has made it plain that he wants to be a heavy hitter in Hollywood, and 106 minutes of extravagant stupidity seems a small price to pay. After spending \$1 billion in 1993 to buy two major production companies, Turner Broadcasting System Inc. is ponying up \$750 million more to produce 39 feature films this year.

Like many of its megamedia rivals, Turner is seeking lively "product" to fill its various distribution channels: the TBS and TNT cable networks; a growing licensing and merchandising division;

and—someday, perhaps—a broadcast network. Turner also needs to freshen up the list of 3,400 titles it picked up in its 1986 acquisition of the MGM film library.

But if Turner's strategic reasons for plunging into filmmaking are clear, some observers say the company risks running into the same problems that have bedeviled Japan's Sony Corp. and other babes in the Hollywoods. For one thing, Turner's three production companies—New Line and Castle Rock Entertainment plus homegrown Turner Pictures—are making their big push just as Tinseltown faces a deluge of new titles. Under new management, MGM and Paramount are also ramping up their production schedules.

"FAUSTIAN DEAL." What's more, Turner is tinkering with the successful recipes of his studios by boosting their film budgets and changing their development slates. New Line Chairman Robert K. Shaye, who built his company on horror films and other low-budget flicks, has already plunked down \$4 million each for scripts by screenwriters Joe Eszterhas and Shane Black. Castle Rock, which nurtured a reputation for pro-



Turner is making more movies partly to develop product for his cable networks, merchandising operation, and—maybe—a broadcast network

ducing a small number of high-quality films, is expanding its annual output from 6 to 12 films. "You can go broke in this town asking people to go against what made them famous in the first place," says one producer.

That comes on top of other unavoidable hurdles. Buying Castle Rock gave Turner access to the prodigious filmmaking talents of Rob Reiner, one of the company's founders. But Columbia Pictures retains home-video rights to Castle Rock's films until 1996 and will continue to distribute the films until at least 1997. So Turner's revenues are severely limited. "That's part of the Faustian deal we made to get Castle Rock," admits Scott M. Sassa, the 35-year-old president of Turner Entertainment Group. "It's a weakness." Meanwhile, New Line is riding high with Carrey's *The Mask* and *Dumb and Dumber*. But the company hasn't proven it can turn out non-Carrey hits to justify its growing budgets. Turner Pictures, which produced the money-losing historical epic *Gettysburg*, hopes to do better through a six-picture deal with producer Dawn Steel.

LICENSING QUEST. Then, too, the mercurial Turner has to contend with a clutch of formerly independent egos. "We've got a bunch of proud peacocks all thrown into the same barnyard," says New Line's Shaye. "So far, the pecking is at a minimum." Sassa concedes ego clashes are inevitable. But he hopes to work them out in monthly meetings with the heads of the film units at Atlanta headquarters.

Turner's film business is still a small piece of his empire. The three movie units turned in an operating profit of \$57.5 million last year, estimates Seidler Cos. analyst Jeffrey B. Logsdon. That's a skimpy 6% return on Turner's \$1 bil-

lion investment. Logsdon believes movie production will log a \$100 million profit this year, hardly a blockbuster performance. By contrast, Logsdon predicts that Turner's entertainment networks will generate \$238 million, while his news operation will make \$245 million.

Clearly, though, Turner has grander ambitions. His \$750 million production budget exceeds the company's total projected 1995 cash flow of \$550 million. Turner executives say they will finance that cost by taking on some additional bank debt. At \$2.4 billion, Turner's debt is six times its 1994 cash flow—putting it in the same leverage league as such

But to make this synergy really happen, Turner's studios are going to have to turn out winning films. Sassa notes that keeping the three studios separate allows each to troll for talent. And Turner's well-publicized higher budgets should draw top names. "I don't think there's anyone in town who would say that they wouldn't come work for us," declares Castle Rock chief Alan F. Horn. Indeed, stars such as Al Pacino, Susan Sarandon, Billy Crystal, Sigourney Weaver, Marlon Brando, and Morgan Freeman will all appear in Turner titles this year.

PEACOCK HUNTING. Turner is forgoing some other expensive Hollywood trappings, though. His three production companies all lease studio space. "Too many people want to sit in Irving Thalberg office and own a studio lot," says Terence F. McGuirk, executive vice-president of TBS. "We don't have that intention. We're in the movie business for strictly strategic reasons."

There's one final element to Turner's multimedia strategy: broadcast television. Turner is angling to acquire part or all of NBC from General Electric Co. Combining CNN with an existing TV network's news division would save TR

\$100 million in production costs. NBC would also boost Turner's muscle in bidding for sports properties such as National Football League telecasts. And it would enable Turner to tap directly into the big advertising money that comes along with premier and repeat airing of feature films on TV. "We've got a unique model that bodes well for us if we ever gets into a bidding war," says one source close to Turner.

Before Turner can even enlist in any such battle, though, he will have to overcome objections from Time Warner, which, along with Tele-Communication Inc., bailed out a cash-strapped TBS in 1987. The two now control 20.5% of the company's voting shares and can veto any major acquisition or sale.

Turner's network aspirations may look like a long shot now. But they're alive enough that the GE board discussed the Turner bid at its December meeting. Turner ever does end up owning NBC or another network, his Hollywood strategy may end up looking as smart as his current films look dumb.

By David Greising in Atlanta, with Ronald Grover in Los Angeles

TED'S EXCELLENT ADVENTURE?

Key pieces of Ted Turner's film empire

	COST	RECENT FILMS	UPCOMING SLATE
NEW LINE CINEMA	\$682 million (stock and assumed debt)	<i>Dumb and Dumber</i> , <i>The Mask</i>	<i>Don Juan de Marco</i>
CASTLE ROCK ENTERTAINMENT	\$384 million (cash and assumed debt)	<i>North, City Slickers II</i>	<i>Forget Paris</i> , <i>City Hall</i>
TURNER PICTURES	Startup	<i>Gettysburg</i>	<i>Angus</i>

DATA: COMPANY REPORTS

heavily-indebted media giants as Time Warner and Viacom.

Turner is spending big to crank out the celluloid because the rest of the Turner empire is poised to capitalize once the movie studios go into full production. Consider Turner Pictures' upcoming film *Jonny Quest*, which it plans to release in the summer of 1996. Turner's publishing, interactive-media, merchandising, and licensing executives will also unleash a raft of products based on the cartoon hero. "*Jonny Quest* will be a consumer-products bonanza," says Philip Kent, president of Turner Home Entertainment.

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THE MAN WHO'S DRIVING FIAT LIKE A FERRARI

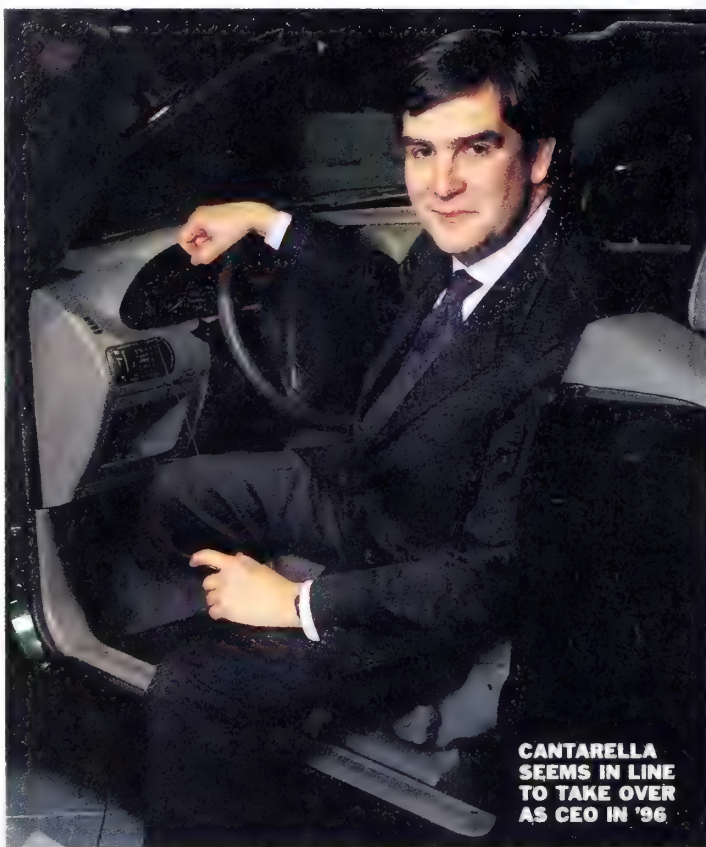
With the Punto a runaway hit, Paolo Cantarella has the carmaker roaring again

After putting in a 55-hour week running the car operations of Fiat, Paolo Cantarella doesn't just sit back and relax. Come the weekend, he invariably tries out a competitor's car on the narrow Alpine roads above Fiat's hometown of Turin. One cold December Saturday, it's the turn of the new Polo, the snazzy subcompact from archrival Volkswagen. "I try them all," says Cantarella, who describes himself as "car crazy."

Such devotion is helping to turn around Italy's largest company, which just two years ago seemed on the verge of disintegration. A five-year program launched in 1991 and shepherded by Cantarella to produce new models is starting to pay off. Fiat's sleek new Punto subcompact is the runaway star of the European auto industry, scooping up more than 680,000 orders in 1994. That's making Fiat a tough rival again for Volkswagen, Peugeot, Renault, Ford, and General Motors. Although Fiat's share of the European market has slid to 10.4%—down from 15% in the late 1980s—the Punto's success is helping Fiat rev up sales in key markets like France and Germany.

CROWN PRINCE. With its \$20 billion car operation healthy again, Fiat will rack up net profits of around \$600 million for 1994, after a loss of \$1.1 billion in 1993. And profits could more than double in 1995. There are still risks, of course, but Fiat's future looks brighter than it has in years.

The turnaround bodes well for Cantarella, too. The 50-year-old engineer—who likes to spice his conversation with phrases in earthy Piemontese dialect—is increasingly seen as the heir apparent to



CANTARELLA SEEMS IN LINE TO TAKE OVER AS CEO IN '96

71-year-old Cesare Romiti, Fiat's tough CEO since 1976. Romiti and Chairman Giovanni Agnelli are both expected to step down in mid-1996. If he ascends to the CEO's post, Cantarella will be running a \$40 billion giant with interests from publishing and sports to railroads and defense.

Cantarella's influence was felt even before he got the top job at Fiat Auto

IN THE BLACK After its worst-ever loss in 1993, Fiat netted \$600 million in 1994

four years ago. As head of supplies and distribution in 1989, he cut the number of main suppliers from 500 to 120 and encouraged big vendors to integrate their operations with Fiat's. At Fiat's brand-new plant in the Southern Italian town of Melfi, major suppliers to the Punto built plants on-site—a concentration not even Nissan Motor Co.'s ultramodern plants in Britain match.

Cantarella's Fiat has also gone further than Euro-rivals in adopting another practice popular among the world's best carmakers: co-designing parts with its main suppliers instead of developing them exclusively in-house. Suppliers co-designed half of the Punto's components, cutting the number of parts Fiat must ultimately assemble. Sila Group, a \$75 million maker of car cables, now supplies Fiat with an entire pre-assembled gearbox system

for the Punto—reducing the final costs by at least 15%. "It's not only cheaper, it's easier to manage," says Sila Chairman Oreste Brero.

Transforming Italy's traditionally conservative shop-floor practices has also been key. At Melfi, for example, Fiat slashed the layers between plant managers and workers and spent \$64 million training its 7,000 workers and engineers to work in small teams. Now, the 31 independent teams—with 15 to 100 workers apiece—oversee car-assembly tasks from start to finish. Cantarella's challenge is to spread the Melfi gospel through Fiat's older, more hidebound plants in the North.

Such innovations have helped cut the time Fiat takes to get new models to market—from 60 months in the 1980s to

panese-like 36 months. It's the fastest rate in Europe. As a result, nine models have hit the market since 1992, giving Fiat a fresher look than rivals just as Europe's market is expected to hit 12.5 million cars this year—is coming out of low gear. Fiat may be a laggard,”

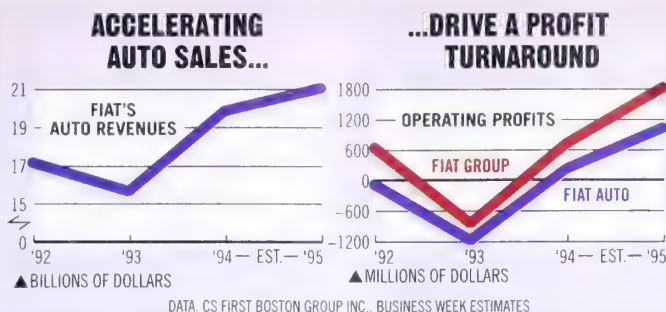
John Lawson, an auto analyst at DRI/McGraw-Hill, says Fiat may have become a leader.”

The improvements come none too soon. The \$1 billion-plus loss in 1993 was Fiat's worst results ever. With its aging product line crumpled by an onslaught of foreign competition, the company's share of its home market slipped from 60% to 45%. And the Italian car market, traditionally Europe's best after Germany, sank by a stomach-churning 30% over the past two years in the face of economic and political upheaval. The company desperately sold pieces of its diversified holdings to shore up its auto core. Debt, meanwhile, rose 40%, to \$4.5 billion.

WEAKER LIRA. The burden of that debt hangs Cantarella cannot afford any false promises. A critical moment will come next September when Fiat unveils a new size model to replace its six-year-old Tipo. The midsize market is Europe's most lucrative—and most hotly contested, with models such as Adam, VW's Astra, VW's Golf, and Renault's Megane. The Tipo, which sold only 130,000 units last year, compared with 740,000 for VW's Golf, has long trailed the segment leaders. But insiders say that the new replacement, which cost \$1.3 billion to develop and is code-named 182, will be packed with new features. If combined sales of the Punto and 182 hit 1 million units a year, says Chairman Agnelli, “that will guarantee the future of Fiat.”

Several developments could threaten Fiat's future, though. Even in a strengthening market, competition is ferocious. Cantarella points to Toyota ads in Italian newspapers offering 18-month payment terms at zero interest. Ford Europe—suffering from a sharp slide in sales in the key British market since 1992—has successfully taken aim at Italy with its new Fiesta. And Fiat's rich lineup of models could be matched by others. In Europe, one of every four cars in 1993 may be replaced by a new model.

But rustling rivals aren't the only threat. Far, Fiat's exports have benefited immensely from a devalued lira. But a long-awaited upturn in Italian sales may be materialized if inflation soars and domestic interest rates keep rising—both of which possibilities, given Italy's political



instability and huge deficit. And after more than two years of labor peace at Fiat's plants, there are rank-and-file rumblings for fatter paychecks. Fiat shares, among the best performers on the Milan bourse last year, have slumped 15% in recent weeks.

Overseas expansion offers a buffer against Italy's disorder. Fiat is the No. 1 carmaker in Brazil, Poland, and Turkey and is busy cutting deals on plants

everywhere from India to Mexico to the Gaza Strip. “These are areas with quickly growing economies and young populations,” says Cantarella. The new markets take fully one-third of Fiat's output, exports within Europe another third, and Italy the rest. That's a far cry from the 1980s, when Fiat depended on Italy for more than half

its sales. And while such internationalization is now fired by the weak lira, it's here to stay, Cantarella says. Ever cautious, Cantarella won't say that the group has turned the corner. “I would say Fiat's getting better,” he allows. But there's a new, more confident feeling in the air. Even as much else in Italy seems to be going wrong, in Turin something is going right.

By John Rossant in Turin

STRATEGIES

'A LOT OF THE WEAKNESSES CARBIDE HAD ARE BEHIND IT'

Downsized with a vengeance, it's cranking out fat profits

On a wooded hill overlooking Danbury, Conn., sits a monument to the Conglomerate Age. Built in the 1970s to hold 3,000, the 1.3 million-square-foot headquarters of Union Carbide Corp. now houses just 500. A decade ago, Carbide employed 110,000 and sold \$10 billion worth of Eveready batteries, Glad bags, and countless industrial chemicals. It was an unwieldy, barely profitable mishmash.

Then came the accident in Bhopal and a failed takeover attempt by the raider Samuel Heyman. Having borrowed \$3 billion to fend him off, Carbide was left with an 80% debt-to-capital ratio. Survival meant slimming down. “We had too many diverse businesses competing for capital and management attention,” says Robert D. Kennedy, Carbide's CEO since 1986.



KENNEDY: “We were in too many diverse businesses”

Kennedy, a lifelong Carbide executive who formerly ran the chemicals-and-plastics division, took out the knife. He sold assets such as the battery and consumer-products units, brought debt under \$1 billion, and shed 90% of the workforce. Even the building was

Saddled with high costs, Union Carbide sold off units, cut its debt in half, and shed 90% of the workforce

sold. By 1993, Kennedy had wrung \$575 million out of overhead. Revenues were halved, to \$4.6 billion, but pretax profits from operations—a 36% increase from 1992, to \$242 million—were finally up.

Then, as the cyclical chemical business turned in a big way last year, Carbide soared. Third-quarter pretax profits jumped 122%. For the full year, S.G. Warburg analyst Paul Raman expects pretax income to rise 89%, to \$457 million, on sales that are up 6.5%, to \$4.9 billion. Now at 30, Carbide's shares rose 31% in 1994, best among the 30 stocks in the Dow Jones industrial average.

Of course, most chemical companies are riding the same tide. Rivals such as Dow Chemical Co. and DuPont Co. have also cut costs and seen sharp earnings gains. But because Carbide has been paring costs far longer, says Robert Bauman, vice-president of Tarrytown (N.Y.) consultants Chem Systems Inc., it is better positioned to make the most of the cyclical upturn. Moreover, Carbide's cost-cutting, combined with new production technology, should keep Carbide profitable in the next downturn—and help boost Kennedy's plans to expand abroad.

TRAPPED. That's some change. Indeed, Carbide's early improvement masked an ugly fact: Profits in 1992 and 1993 all came from cost-cutting. With 50% of revenues now coming from polyethylene and ethyl glycol—commodities used in everything from garbage bags to polyester and antifreeze—Carbide was trapped in the down cycle. Its core business made little money.

No longer. Since late 1993, demand has been soaring, while chemical inventories have fallen dramatically. The result: Ethyl glycol prices jumped 25% in 1994, while polyethylene skyrocketed

by more than 50% (chart). That's one reason for Carbide's quick turnaround: Huge fixed costs mean marginal price hikes yield huge gains. Raman estimates that each time polyethylene rises a penny a pound, Carbide adds 15¢ profit per share—and prices have been rising 2¢ to 3¢ a month. "Carbide is now the low-cost producer in both key markets," he says. "They have tremendous leverage."

Carbide wasn't always the low-cost producer—far from it. But after Kennedy sold most of Carbide's noncore assets in 1990, he launched an aggressive strategy to squeeze out excess overhead. Centralizing inventory management and improving distribution slashed inventory and shipping costs. Plant maintenance was revamped, saving \$60 million annually. Better cash management cut financing costs, saving \$65 million. Kennedy sold Carbide's two corporate jets and gave up his chauffeur. Even rivals are impressed: "If you go back two years, Carbide was not that well thought of, but their return in 1994 was tremendous," says William H. Westendorf, president of Huntsman Specialty Chemicals Corp. "A lot of the weaknesses Carbide had are behind it."

Of course, the thing about cycles is that they keep turning. Demand and pricing for chemicals are expected to weaken through 1995. Kennedy's goal is to keep squeezing costs so that Carbide can remain profitable when the market drops. One key part of the strategy: Carbide's Unipol processing technology, which reduces the steps to convert raw materials into chemicals. Because the energy-efficient technology permits chemical reactions to occur at lower pressure than normal, Carbide claims it cuts operating costs 25% to 40%. That helps Carbide compete with rivals such as Mobil Oil Corp. that own

the petroleum feedstocks that Carbide has to buy.

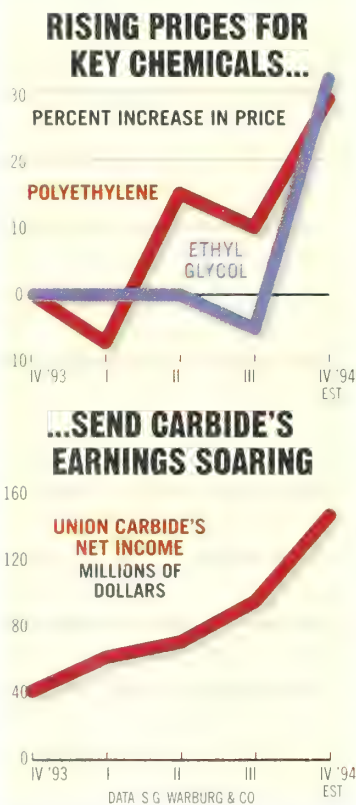
But cutting costs isn't Kennedy's only goal: Carbide is also using its technology as a wedge to crack foreign markets. Carbide left Europe in the early 1980s because it couldn't compete with oil-rich rivals such as British Petroleum Co., but it recently formed a joint venture with Italy's Enichem. Carbide's technology will be used in a new polyethylene plant that will replace existing high-cost Enichem capacity. Deals have also been struck with France's Elf Aquitaine and Britain's ICI. Observers say Carbide's low-cost technology should allow it to gain share just as several years of chemical industry consolidation give way to growth. "Carbide seems to have caught the timing right," says one London consultant. Although 70% of sales are now in the U.S., "the balance will shift rapidly abroad in the next few years," says Kennedy.

CHEAP OIL. To tackle Asia's plastics market, Carbide is building a \$1.5 billion petrochemical complex with Kuwait's government. The deal gives Carbide proximity to Asia and access to low-cost oil needed to compete there against Saudi Arabian petrochemical makers. Kennedy claims that the Kuwaiti plant will be among the world's cheapest when it comes on line in 1997.

Growth could also come from putting Carbide's technology to work making higher-value products. In October, Carbide announced plans to build a synthetic-rubber plant using the Unipol process. Kennedy wants to use such rubbers—which go into items such as roofing tiles, window frames, and gas tanks—to supply the auto-parts and housing markets. Still, competitors are unlikely to let Carbide expand without a fight. Kennedy has also increased capital expenditure to boost Carbide's small but profitable business in solvents and additives for paints and coatings. These are part of Carbide's noncyclical side, which contributes a steady \$300 million a year to income and buffers the company during down cycles.

Of course, Kennedy is hoping he won't need as much buffering in the future, given Carbide's newfound profitability in commodity chemicals. Still, a little insurance never hurt.

By Tim Smart in Danbury, Conn., with bureau reports



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America's Cup '95: Forget wooden ships and iron men (or women)



Winfried Feifel designs wings for tomorrow's supersonic jets. But for much of the past year, the Boeing Co. engineer has been using his knowhow to help create something a bit slower: a keel for Young America, one of three U.S. boats competing for the honor of defending the America's Cup. Feifel's task is to help find the right arrangement of lead weight and streamlined wings under the hull to make the Roy Lichtenstein-painted contender speedier and more maneuverable than its rivals. And from Jan. 12 through May

spell defeat, the America's Cup still demands the world's best: sailors such as four-time winner (and 1983 loser) Dennis Conner of the U.S. and New Zealand ace Chris Dickson. But these days, even the savviest salt needs to ride the waves of innovation. "Unless you have leading-edge technology in boat design, structural engineering, sails, and electronics, you simply can't compete," says John Marshall, president of the Partnership for America's Cup Technology 95 (PACT 95), the business-backed group behind Young America. Of course, sheer

MAINSAIL OF TOMORROW? *Young America catches the wind*

luck sometimes takes the tiller—for good or for ill. On Jan. 4, for example, a mini-tornado ripped through the PACT 95 compound, damaged Young America, and left the team scrambling.

This year's race is the most technology-driven in the Cup's 144-year history, in part because of two related trends. First, few of the teams can afford the \$68 million spent by businessman Bill Koch to build four boats along the way

to defending the Cup in 1992. This year, Koch's total budget for America's Cup, which has an all-female crew, is \$20 million, less than half of which is coming out of his own pocket. PACT 95 is spending \$17 million, Conner \$15 million. Second, advances in technology have helped bring costs down. Software developed by such companies as Boeing and San Diego defense contractor Science Ap-

A SHIP CHANDLER'S LIST FOR THE INFORMATION AGE

HULL Scores of designs tested in computer simulations. Team Dennis Conner tapped GM engineers to lighten a carbon-fiber hull, PACT 95 used computer code to design a radical internal structure.

KEEL The basic design—long keel with lead bulb at bottom—refined by computer, then perfected in wind tunnel. Both PACT 95 and Team Conner rely on Boeing engineers.

SAILS Most boats use one-piece molded sails—stronger, lighter, and faster than sails sewn from cloth.

INSTRUMENTS Video cameras, satellite navigation, ultrasonic wind-speed detectors, laser gyros, and advanced software tell sailors everything from their exact position to how the wind is changing.

DATA: BUSINESS WEEK

In races where a single botched sail change missed wind shift can

tions International Corp. has made possible to test scores of hull and shapes on computer-simulated waves quickly and cheaply. As recently as a decade ago, cumbersome and costly wind-tunnel and water tests limited architectural options to three or four designs. But "this year, it's more like 10," says Alan Ramadan, managing director of Fluid Thinking, a Melbourne company set up not only to win the cup in Australia but also to commercialize simulation technology.

Testing on the cyberseas is paying off. When Dennis Conner first sailed his *Stars & Stripes* in late November, the boat's speed and performance in a variety of conditions uncannily matched predictions made by a computer program based on Microsoft Corp.'s Excel. PACT used an award-winning program developed by Altair Computing Inc. in Troy, Mich., to help design the internal structure of Young America's carbon-fiber hull. The program devised a spaghetti maze of tubes to supplant traditional bulkheads and plates. "It looks like a pipe and scarf," says Marshall. But the light—which makes the boat faster.

SAILS GALORE. The breakthroughs aren't limited to hulls. Most boats will be powered by revolutionary sails invented by two Swiss engineers and developed by North Sails Group in Milford, Conn. First, sailmakers place a film over a full-size mold of a sail. Then, they lay down a web of threads, precisely oriented to withstand predicted stresses. A final layer of film follows. The sandwich is glued together, creating a piece, almost-transparent sail that is 10% lighter than a sewn-cloth one. The reduced weight boosts speed, and the sail also springs back into shape after a tack—for quicker acceleration. That's a big advantage in match racing, where competitors may tack 30 times on a single upwind leg. It's also a reduced business risk for North Sails, which is building a big automated plant in Minden, Nev., in hopes that a Cup victory by a contender using its designs will spur the other kind of sales.

Helping the 16-member crews wring every last knot of speed from this technology is a dazzling array of sensors: cameras to monitor sail shapes, satellite receivers to pinpoint position, and laser gyroscopes to measure every yaw, pitch, and roll. "The more you can provide these talented sailors with relevant information, the better chance they have of making the right decision," explains Australia's Ramadan.

Perhaps the snazziest new sensor is an ultrasonic wind-speed detector. Unlike traditional masthead anemometers, which may take a dozen seconds to respond after a tack or a wind shift, the

device reacts in a split second. Data from the gyros and other sensors let crews spot wind shifts almost instantly, even during intricate prerace jockeying. "If I can pick up a five-degree wind shift first, I can win the start and get a big advantage," says James C. Marshall of Ockam Instruments Inc. in Milford, Conn., which is supplying sensors and software to several teams.

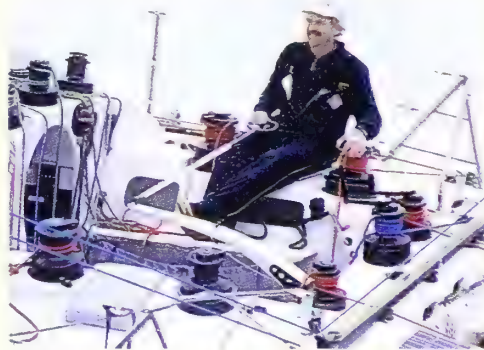
The effect of all this high-tech wizardry may be to put the premium—and the burden—back on the skills of those

at the helm. Unlike in 1992 or 1983, when winners America³ and Australia II had big technological edges, this year's leading teams—Young America, *Stars & Stripes*, *oneAustralia*, and Dickson's New Zealand entry—have all dipped deep into the technology well. "The boats are getting closer and closer," says Massachusetts Institute of Technology professor and America³ design director Jerome H. Milgram. "This one is going to be won on good sailing."

By John Carey in Washington

ROUND THE WORLD BY GRIT, STARS—AND IBM

When Steve Pettengill sold his Florida-based trucking company in 1986 to pursue a career as a long-distance yachtsman, he didn't realize that navigating cyberspace would prove as vital as trimming sails. But during the first leg of the arduous BOC Challenge—a solo, round-the-world race that, like the America's Cup, continues through May—Pettengill discovered the power of the Telecommunications Revolution.



PETTENGILL: Sailing in cyberspace, too

Before the race started on Sept. 17 in Charleston, S.C., a powerful computer system that can receive and analyze satellite weather pictures had been installed aboard his 60-foot craft, *Hunter's Child*. Weeks later, as he cruised off the coast of Brazil, the 43-year-old sailor found himself spending up to three hours a day at the computer, poring over cloud pictures and sea-surface temperature data. At one point, he spotted a high-pressure center with low winds dead ahead, bore off to the west to skirt it, and gleefully watched his less informed rivals sail into the doldrums. "I'm not a big computer person," says Pettengill,

now in second place after arriving in Sydney on Christmas Day, "but I'm sure getting a quick learning curve."

Single-handed racing still pits one sailor against the fickle sea, but in the 1990s, the ocean is a lot less lonely. For companies such as Trimble Navigation Ltd. and Comsat Corp., which are among those behind the technology, the race is a chance to strut their stuff. Pettengill, for example, is sponsored by privately held Hunter Marine Corp. in Alachua,

Fla., one of the world's leading sailboat makers. Chairman Warren R. Luhrs, himself a renowned long-distance sailor, believes his racing exploits helped Hunter's market share soar during the recent recession, while many rivals sank.

BEYOND GIZMOS. Still, no amount of technology can tame an angry sea. The winner of the race's first leg, France's Isabelle Autissier, 37, lost her mast in a storm east of Cape Town. She managed to replace it, only to lose the entire boat later. Tumultuous seas also battered *Hunter's Child*. One storm rolled the boat so violently that the masthead plunged into the ocean three times, the boom broke, and water smashed a gaping hole in the cabin. Fortunately, Pettengill was able to repair the damage.

Of course, there were still a few glitches. The water that poured into the cabin soaked Pettengill's IBM laptop, knocking out half its keys. Since the machine provided his fax-link to shore, he says, "I sent some pretty strange messages." Waterproof computers—now there's an idea for you, Lou Gerstner.

By John Carey in Washington

THE SWAT TEAM OF BIAS LITIGATION

Oakland's Saperstein law firm is leading a new rush of employment-discrimination suits

In late December, seven women stood before TV cameras and charged their employer, Atlanta's popular superstore chain Home Depot Inc., with sexual discrimination. Cheryl L. Williams, 41, told how she trained two young men in the flooring-and-tile department at a store in Corona, Calif. Soon afterward, despite good performance reviews, Williams says she was laid off, and the two men got her job. Then, Jacqueline Genero, 22, explained how managers asked for a recount after she was voted the first female Employee of the Year by fellow workers in 1993. Although she won on recount, Genero claims she was denied the traditional \$500 prize.

These and other incidents provide the basis of an employment-discrimination class action filed against Home Depot. Plaintiffs claim they will expose a company that fails to train, promote, and pay fairly its female workers. "Women's employment opportunities are determined not on the basis of their interest, experience, or abilities, but on the basis of their sex," says the plaintiffs' lawyer, Barry Goldstein.

BIG COMEBACK. Home Depot says it has launched an internal inquiry and is taking the lawsuit "very seriously." It ought to. The Oakland (Calif.) firm representing the plaintiffs, Saperstein, Goldstein, Demchak & Baller, has collected more than \$600 million in damages and legal fees from companies its clients have sued for discrimination over the past three years (table). Their winning formula:



DISMISSED AT DEPOT: Williams says her job went to men she trained

target high-profile corporate defendants and use elaborate statistics to make the case.

Saperstein isn't just bringing in big paydays for its partners. It's also spurring other lawyers and disgruntled workers into action—so much so that employment-discrimination class actions are making a comeback. After two decades of decline, the number of such lawsuits filed last year jumped 30%—from 39 in 1993 to 56 in 1994, according to the Administrative Office of the U.S. Courts.

Recent changes in legislation are also encouraging such cases. The Civil Rights Act of 1991, for instance, for the first time allowed for punitive and compensatory damages of up to \$300,000 per person—in addition to back pay—in employment class actions. And years of activism aimed at equality on the job are bearing fruit. "We're seeing more groups of women come forward," says Kathryn B. Dickson, an Oakland lawyer currently suing Chevron Corp. for gender discrimination.

Of course, compared with the 1970s civil rights litigation boom, in which employment class actions hit an annual high of 1,174, the current wave looks small. But consultants and lawyers are advising corporate clients to watch out. Despite programs to promote workplace diversity, "in the current environment no company is immune from these lawsuits," says Peter C. Robertson of Organization Resources Counselors, which tracks employment-related class actions.

And few law firms make executive squirm the way the 14-lawyer team at Saperstein does. "Getting a summons from you is like getting a call from 60 Minutes," an attorney once told Goldstein. The firm has corporate radar screens with a case against State Farm General Insurance Co., charged with denying 1,000 women jobs as agents. When the company settled for \$250 million in 1992, it was an achievement that had been 13 years in the making. Partners at Saperstein, working on a contingency-fee basis, had even taken out second mort-

SAPERSTEIN'S CLASS ACTIONS HIT PAY DIRT

DEFENDANT	SETTLEMENT	DATE
STATE FARM GENERAL INSURANCE	\$250 million	1992
SHONEY'S	\$132.5 million	1993
LUCKY STORES	\$107 million	1994
FLAGSTAR/DENNY'S	\$54 million	1994
ALBERTSON'S	\$29.5 million	1994

DATA BUSINESS WEEK

s on their houses to cover expenses. Among the most effective—and most expensive—of Saperstein's tactics is to inspect corporate records on hiring, promotion, and pay raises. Specialists in firm and computer-savvy consultants use the data, usually kept on huge microfilm tape reels, to identify discriminatory patterns. In the State Farm case, consultants spent 2,000 hours auditing employment records.

For years, the complexity of these suits kept all but a handful of dogged plaintiffs and devoted lawyers out of court. But other lawyers have watched Saperstein rack up big settlements and take a piece of the action. Houston's Robert S. Bennett, a general business lawyer, initially brought a race-discrimination case against Fort Worth's Color Tile Inc. chain in 1992 on behalf of a female plaintiff. But a Saperstein class action, charging Denny's restaurants with refusing to serve African-American customers, gave Bennett the idea to seek class-action status in the Color Tile case. The Denny's case "was kind of inspirational," he says. Color Tile attorney David D. Inman says the court isn't likely to grant class-action status.

POSTERS. Lawyers are also breaking some new ground. In 1993, a sexual harassment case for the first time achieved class-action status. Sprenger & Gering in Minneapolis brought the case, charging Eveleth Mines in Duluth, Minn., with allowing male workers to view nude posters and graffiti identifying female "hot spots" on its office walls. Eveleth did not return calls seeking comment.

Other such suits have been denied class-action status. In a case against Chevron, plaintiffs told a federal judge that a pornographic E-mail was sent to personal computers at Chevron's information-technology division, including a picture of a bound woman with the caption "Taming of the Arrogant Little Bitch." But the judge ruled that harassment claims cannot be brought collectively because they are based on individual experiences. Chevron says: "We do not tolerate discrimination or harassment in the workplace."

The pressure brought to bear by suits such as Saperstein does lead to change, not just costly legal woes. At State Farm's Inc., 25% of management positions today are held by minority-group members, up from 14.5% in 1989, when the firm was first sued. At State Farm, two of the five agents hired in the wake of the suit have been women. Companies don't want to review their own employment records before Saperstein does for them.

By Russell Mitchell in Oakland, Calif., with Jonathan Ringel in Atlanta

'I SAW MY JOY CURVE FLATTENING OUT'

Class actions have been good to Berkeley (Calif.) lawyer Brad Seligman. A former partner at the firm now known as Saperstein, Goldstein, Demchak & Baller, he was instrumental in winning huge settlements against State Farm insurance, Shoney's restaurants, and the Lucky Stores supermarket chain. But after 10 years at the firm, Seligman left in 1991 "with more money than I ever dreamed of, expected, or even wanted."

Now, he's giving a chunk of it away. Seligman is using \$1.25 million of his undisclosed fortune to seed the nonprofit Impact Fund, which he created in 1993. Dedicated to funding class actions in civil rights, environmental, and poverty law, the Impact Fund hands out grants of up to \$50,000 to attorneys. They repay the money only if they win.

Seligman, 43, says he would like to reverse the dramatic decline in public-interest class actions that has taken place since the late 1970s and counter the cuts in legal services to

of Supervisors in 1993 and force the creation of voting districts to give the Latino community more voting power. Avila says that money is a serious problem and that grants "make a big difference."

SIXTIES DREAM. Another Impact grant is challenging waste-incinerator-siting practices in Michigan, which Seligman says discriminate against the poor. "Mainstream environmental groups are good at protecting the wilderness," he says. "We want to protect the rights of poor people." The Impact Fund is targeting corporations, too. For example, it is funding a race-discrimination suit against Food Lion Inc. supermarkets and a disability-discrimination case against USAir Inc. On his own, Seligman is pursuing a case against United Artists for allegedly failing to provide adequate seating for the disabled at its movie theaters.

Seligman grew up in Hollywood, the son of a lawyer. But while bouncing around different colleges in the Bay Area, he became a "very political late '60s, early '70s type," he says. He still wears a beard and keeps his hair bushy. And he chose the name of his daughter, now 13, from the blues song *Corina*. For fun, Seligman plays the guitar in a recording studio that he installed in his house in Berkeley.

Although many years have gone by, Seligman still bears the rebel streak that made him resist his father's urging to go to law school—"until it was my idea." Richard Drogin, a statistics professor who consults for the Saperstein firm, says Seligman quit his partner-

ship because "he felt the direction [at Saperstein] was getting too corporate." Seligman says: "I saw my joy curve flattening out." But with his comfortable nest egg, he is able to live out a '60s dream: supporting public-interest law by day and jamming away in a personal recording studio by night.

By Russell Mitchell
in Berkeley, Calif.



SELIGMAN: Handouts to class-action plaintiffs

the poor. Part of the problem is that private foundations have stopped funding class actions while the cost of litigation has continued to skyrocket. "There is a lot less money out there," he says.

One lawyer who received Impact Fund money is Joaquin G. Avila of Milpitas, Calif. He used a \$35,000 grant to help win a class action against the Monterey County Board

PASSAGE TO INDIA, COMPLIMENTS OF GEORGE

Purnendu Chatterjee is running a billion-dollar Soros fund despite a run-in with the SEC

Everyone from his boss to his secretary calls him P.C., with affectionate informality, and his understated manner can be almost nerdy. Yet 45-year-old Purnendu Chatterjee inspires respect—and sometimes fear. For 10 years, global investor George Soros has taken small stakes in Chatterjee's lucrative turnaround ventures in the U.S., mostly tiny companies with a technological niche. Now, at the helm of Soros' billion-dollar Quantum India Fund, Chatterjee is making waves in the country of his birth. For Soros, Chatterjee means easier entree into one of the world's most promising but most regulated emerging markets. And the Soros connection puts ample resources at Chatterjee's disposal.

The return of this native son to his homeland, trailing a world-famous investor's dollars in his wake, is the latest career move for a man marked by controversy. As recently as January, 1993, Chatterjee was dealing with a Securities & Exchange Commission allegation of insider trading. A few years earlier, a takeover target took him to court. Yet Soros' New York headquarters is now home to the Chatterjee Group, an affiliate of Soros Fund Management. And even before naming him as principal adviser to the new India fund, Soros appointed Chatterjee to co-manage the \$1.5 billion Quantum Industrial Holdings Fund and \$500 million Global Power Investments, two funds aimed at investing in emerging markets.

Canny, meticulous, and at home in both Anglo and Indian cultures, Chatterjee has obviously proved himself to Soros, despite his run-in with the SEC. Says Anupam Purie, who heads McKinsey & Co.'s Indian operations and used to work with Chatterjee: "P.C. is smarter than anybody else I know, by a factor of at least 10." George Soros declined to comment about Chatterjee and their investments.

Chatterjee was born to a middle-class family in Calcutta and went to one of the prestigious Indian Institutes of

Technology. After getting his engineering PhD from the University of California at Berkeley and working for a while at the Stanford Research Institute, he spent 10 years at McKinsey in the U.S., the last two as a partner. During his tenure there, he married the daughter of Indian steel magnate Viren Shah. He now divides his time between India and New York City, where he keeps a modest apartment overlooking Central Park.

His background clearly benefits him back home, where, despite a gradual liberalization, the government remains wary of foreign investors. Just last month, the Chatterjee Group secured a 26% stake in UB Ltd., a conglomerate with interests in brewing, distilling, pharmaceuticals, engineering, fertilizers, and plastics.

SLEEPING BEAUTY. Soros and Chatterjee scored their first major coup in India last May, when they brought to life the comatose Haldia petrochemical project near Calcutta. For 17 years, the project was a sleeping beauty. Then, P.C. reconfigured Haldia's business plan to provide better cash flow. More important, he brought a \$200 million capital commitment from Soros. Within days, the project's equity structure was finalized: It would be 25% owned by Soros, 25% by the state government of West Bengal, around 8% by India's Tata family, and 42% publicly held. Soros made this move through Chatterjee Petrochemical, a company set up to channel funds to Haldia and based in Mauritius, which has favorable tax treaties with India.

Chatterjee's Progress

1974 Chatterjee receives PhD in engineering from University of California, Berkeley, proceeds to Stanford Research Institute.

1976 Joins McKinsey & Co.; promoted to partner in 1984.

1984 In partnership with George Soros, takes over components maker John Beall & Co.

1990 Shareholders of T-bar, a takeover target, sue Chatterjee and Beall for improper trading; defendants pay \$114,500

1993 Chatterjee pays \$643,855 in an SEC consent decree for insider trading of Foxboro, an electronics company in which he and Soros hold a combined 4.8% stake.

1994 Soros appoints Chatterjee investment manager for the \$1.5 billion Quantum Industrial Holdings, \$500 million Global Power Investments, and \$1 billion Quantum India Fund.

DATA: BUSINESS WEEK



The local press loved it. Besides making much of Chatterjee, the media heralded Soros as a Hungarian Jew who had escaped the Holocaust and took personal interest in India's downtrodden millions. Downstream industry will provide 100,000 jobs for the region where P.C. was born.

With an evolving middle class and a 24% personal savings rate, India now has P.C. excited about retail financial services. In 1994, the Chatterjee Group took a 24% stake in a Calcutta-based brokerage. P.C. has also agreed to in-

\$50 million of Soros' money in the t-management arm of General Insurance Corp., India's largest property casualty insurer. The company expects to launch a series of mutual funds. Bringing First World conveniences to Asia as mutual funds to the Third World always seems to bring out the best in P.C. For example, Phoenix Information Systems, based in St. Petersburg, Fla., had been developing airline reservations software for emerging markets since 1986. It was still floundering in 1992, when P.C. began accompanying Phoenix managers on trips to China, Russia, and India. By late 1994, the joint ventures were in place, the

been as welcome as they were at Phoenix. Chatterjee first met Soros in 1983, when P.C. was a partner at McKinsey and growing restless with consulting. A year later, the two bought a tiny electrical components manufacturer called John Beall & Co. At the time, Soros invested only \$340,000. But he and Chatterjee subsequently used Beall as a vehicle for other investments.

One was a 1986 hostile-takeover attempt of T-bar, a \$50 million computer company based in Wilton, Conn., that eventually fled into the arms of a less hostile suitor. P.C.'s attempts to acquire the company prompted a lawsuit. T-bar alleged that Chatterjee and Beall bene-

prompted the SEC investigation. Soros and P.C. had accumulated a 4.8% stake in the company, and Chatterjee was on the board, when it was sold to a British company in 1990. Chatterjee was accused of supplying inside information on Foxboro, before the sale, to an individual in France and a consultant in Connecticut. He paid \$643,855 in a consent decree with the SEC without admitting any wrongdoing.

BITTER STRUGGLE. Chatterjee developed a reputation for buying companies, getting on their boards, and breaking them apart. Says analyst Thomas Carley of Jensen Securities Co. in Portland, Ore.: "If you look at everything he touched,

there was restructuring, sales of the assets or of the company itself."

Perhaps the bitterest struggle was fought in 1991-94 at Tektronix Inc., a \$1.3 million computer and electronic instrumentation company. Quantum Fund, Soros, and Chatterjee bought into Tektronix at \$18 to \$20 a share, when analysts were estimating the company's breakup value at \$40 to \$42. According to analysts, P.C. gave management an ultimatum: Realize this value or you're history. The Soros group finally capped its ownership at 14.9% of the company in exchange for two board seats.

During 1992-94, a host of divisions were spun off. Says Shawn Willard, an analyst with Charter Investment Group Inc. in Portland, Ore.: "Somebody had to be the bad guy, and P.C. was it. [Tek] had some phenomenal technology, but they had no idea what to do with it." By November, 1994, Tek stock was nearing its breakup value. Soros and Chatterjee began selling at \$35 to

\$37 a share, double their purchase price.

In India, Chatterjee and Soros intend to build companies, not break them up. But they're betting that their synergy will be just as successful in a market where they have to start from scratch. Chatterjee says very little of his own funds are invested in India: "Almost everything is Soros. I need his money." Apparently, there's something about P.C. that George Soros needs, too.

By Louise Nameth and Joan Warner in New York, with Shekhar Hattangadi in Bombay



**CHATTERJEE:
AT HOME IN
BOTH EASTERN
AND WESTERN
CULTURES**

Chatterjee developed a reputation for buying stakes in struggling companies, getting on their boards, and breaking them up. His new mission is to build companies—and industries

of which is expected to be up and running in China by mid-February. When came capital from Soros, Chatterjee, and Quantum Industrial Holdings. They initially bought 1.3 million shares of Phoenix, for 90¢ a share, then committed an additional \$12 million. Ultimately, the Soros group will own 49% of Phoenix—and it holds warrants to purchase shares in the future as little as 72¢. Phoenix shares are currently selling for \$1.31. While P.C. and Soros have made money together, they have not always

fitted from short-swing profits through trading T-bar stock after they had acquired a 10%-plus ownership in the company, violating SEC restrictions against such trading by officers, directors, and 10% shareholders. The court ordered Chatterjee and Beall to pay \$114,500. Quizzed about the case, Chatterjee says he thinks T-bar's lawyers were just trying to buy the company time to get another bid.

It was P.C.'s involvement in Foxboro Co., a \$600 million Massachusetts-based maker of industrial instruments, that

DEALS

WHO SAYS THE CONGLOMERATE IS DEAD?

Not Dover. It has 70-plus businesses and is still acquiring

Late last year, ITT Corp., the quintessential conglomerate, took another step to shed that label by deciding to divest its financial services operations and concentrate on a narrower range of businesses, notably entertainment. It was further evidence of the conventional wisdom of the 1990s: Focus on a few core businesses.

At least one company, however, is thriving by defying the gospel: Dover Corp., a large (\$3 billion in sales) but little-known manufacturer with 54 operating companies engaged in more than 70 diverse businesses, from elevators and garbage trucks to valves and welding torches. Founded in 1955, Dover flouts convention in other ways. Abidingly reclusive, it had refused press requests for interviews for a decade before agreeing to talk with *BUSINESS WEEK* recently.

Its spartan New York headquarters, staffed by just 22 employees, resembles a dentist's office: The cramped reception area features a couple of carved ducks under glass and prints of hunters and bird dogs. Although Dover generally earns high marks for its frugal ways, some Wall Streeters complain that the company is so miserly that prospective investors have to badger it to get on the mailing list for earnings statements.

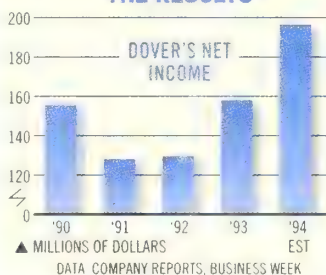
The statements are worth the effort.

Making It Work

THE STRATEGY

- Give near-total autonomy to subsidiary business managers
- Foster risk-taking and entrepreneurship
- Keep headquarters staff and overhead at a minimum
- Buy healthy companies at reasonable prices, retain existing management
- Don't worry about synergy

THE RESULTS



net income of nearly \$200 million, or about \$3.45 a share, according to Zacks Investment Research. Says Chief Financial Officer John F. McNiff:

"Earnings will, as everyone expects, be quite positive."

For 1995, analysts are generally forecasting a 13% increase.

So how does Dover make a conglomerate work? The answer lies in a corporate culture that encourages business heads to manage their companies as if they owned them, conducts an aggressive and opportunistic but disciplined ac-

quisition program, and keeps expenses to an absolute minimum. That formula has consistently produced returns on shareholders' equity in the high teens and average annual total return to stockholders of nearly 14% over the last decade.

More than anything else, Dover is a perpetual-acquisition machine, a case study of the art of the deal. Although Dover's earnings have grown internally at a rate of about 5% to 10% annually, acquisitions have typically propelled earnings growth to as much as 20%. In 1994, Dover spent more than \$180 million to buy 10 new companies, mostly small, low-tech manufacturing and machinery operations such as Midland Manufacturing Co., a maker of safety valves for railway tank cars.

On Jan. 19, analysts look for the company to report record 1994

In his first interview since succeeding Chairman Gary L. Roubos as chief executive last May, President Thomas L. Reece, 52, didn't hesitate when asked if Dover was the antithesis of ITT. "That's how we see it," he said bluntly.

UNCONCERNED. Still, some analysts have begun to wonder if Dover could soon become a victim of its own good fortune. Part of its success has stemmed from its ability to acquire companies inexpensively because they have usually been too small to show up on the radar screens of other potential bidders. Now, however, for Dover to keep growing at its historic pace, says Eli Lustgarten, a PaineWebber Inc. analyst, the size of acquisitions—and the relative prices paid for them—will be forced up. Says McNiff: "I've heard that comment since I joined the company 13 years ago."

If Reece is concerned about his ability to emulate his predecessors, he does not show it. Like all but one previous Dover CEO, Reece, who grew up on a farm in Michigan, rose through the Dover ranks. "I'm not coming in as an agent of change, but as an agent of perpetuation," he says, adding that his management style is barely distinguishable from Roubos'. "He has a mustache and is a better skier," Reece quips.

That said, Reece acknowledges that "we have told managers to be a little more aggressive in growing their businesses." One way company presidents

will accomplish that is by making more so-called "bolt-on" acquisitions than they have in the past. In 1993, for example, Dover bought Phoenix Refrigeration Systems, which makes cooling units for supermarket display cases. Then last year, Phoenix bought Hill Refrigeration Inc., a maker of display cases, enabling the combined Hill

Phoenix to manufacture complete units and compete more effectively with Hussmann Corp., the market leader. To date, Dover has grown mostly through acquisitions of small bu-



CEO REECE: "AN AGENT OF PERPETUATION"

NUTSY BOLTSY Dover favors basic manufacturers that are strong, but smaller than other bidders want

thy stand-alone companies. Typical these companies dominate the business; a market share of 30% or more is unusual, says Reece.

Dover makes little or no effort to create synergies among its holdings. That approach, says Goldman, Sachs & analyst Jack L. Kelly, has helped avoid overpaying for companies because they seem to be good fits. "We take a careful look at anything" with a price-earnings ratio over 15, says Director Magalen O. Bryant, Dover's single largest shareholder.

When buying companies, Dover admits to mistakes. Reece says Dover has ended up divesting only about five. Sometimes Dover's companies get in another's way. One example: Dovatron Inc., a circuit-board assembler. Startup Dovatron found itself competing directly with other circuit-board assemblers that were customers of another Dover unit. Dover spun off Dovatron from shareholders in 1993.

ECONOMY. Dover rarely departs from its practice of granting nearly total autonomy to existing management. Referring to himself and other senior Dover executives, Reece says: "We try to stay out of the way." He boasts that all but 10 out of 22,000 employees are engaged in activities directly related to manufacturing products. The tiny New York City office handles such matters as corporate strategy, finance, and legal affairs.

In contrast to some diversified companies that tend to burden operating units with overhead and stifle entrepreneurial instincts, Dover enables its companies to take even greater risks and move much faster than they could if they remained independent, says William D. Rogerson, president of De-Sta-troy a Troy (Mich.) Dover unit.

Some analysts have criticized Dover for moving too slowly overseas, however. In light of the economic recovery now under way in Europe, for example, analyst Kelly says: "Ideally, you'd like a company with more exposure there than Dover has." But CFO McNiff counters that when its large Dover Elevator Systems division is excluded, more than 30% of Dover's domestic production is exported. And lately, Dover Elevator has negotiated four joint ventures in China, which is expected to become the world's largest market for new elevator sales. At least one source familiar with the elevator industry thinks that Dover Elevator will face stiff competition there, as elsewhere in the overseas elevator market, from established foreign rivals.

So far, though, Dover's powerful conglomerate machine has proved itself more than adept at grinding up the competition.

By Phillip L. Zweig in New York

INVESTMENTS

THE CASE FOR ELECTRIFYING YOUR PORTFOLIO

The threat of utility deregulation may be overblown

They're battered. They're bloody. And, say some analysts, they're bargaining. After a year of being whacked by interest-rate hikes and fears that deregulation would spark brutal price competition, electric utilities seem ready for a comeback. Fears of dramatic deregulation may be overdone. Besides, while competition dims the outlook for some companies, it brightens prospects for others.

Deregulation inspires fear and loathing among investors because it could bring price wars to an industry whose appeal has been its status as a state-sanctioned monopoly. Currently, utilities are able to pass along operating costs. And if a plant has high fixed costs, that will filter into rates, too. Some industrial companies, however, have successfully pressured utilities for discounts. Now, if a concept called "retail wheeling" catches on, other big users may draw

competitive rates from utilities outside their region, then just pay a transmission fee to a local utility. Low-cost producers may gain market share. High-cost producers might have to cut rates.

YEARS AWAY. But the market has overreacted to the threat. T. Rowe Price Associates Inc.'s David J. Wallack, for one, notes that retail wheeling has yet to be approved by any state, although Michigan is experimenting with it. Even if it does become widespread in several years, Wallack argues that rates will not come under as much pressure as the stock market seems to expect. And by that time, he says, the stocks may benefit from a power-supply crunch, since utilities are spending less money on building capacity. Wallack's stock-picking approach: Buy stocks that have been beaten up the most. He likes Centennial Energy, Niagara Mohawk Power, and Pacific Gas & Electric.

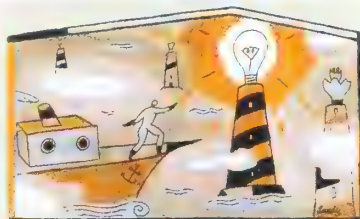
Even if retail wheeling has more impact than Wallack predicts, it doesn't spell doom for all utilities. Investors can profit by focusing on low-cost producers. Kit Konolige, Morgan Stanley & Co.'s electric utility analyst, favors Public Service Co. of Colorado. It has a dividend yield of 6.8%, has a big cost-cutting program, and services a thriving area. He also likes Atlanta-based Southern Co. for its "solid, low-cost operations and growing service territory."

COMEBACKS. PacifiCorp, which operates mostly in Utah and Oregon, may also benefit from competition. "There are some very high-cost utilities in California, with rates almost double those of PacifiCorp," says Barry M. Abramson, Morgan Stanley's senior utilities analyst. "In a deregulated environment, PacifiCorp will have many new opportunities, and they have excess power they could sell into California."

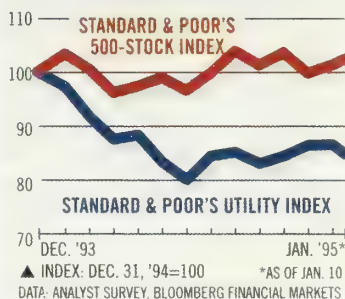
Turnaround situations also warrant attention. Take Illinova Corp. in Decatur, Ill. Its yield is only 4.5%, but its pay-down of debt, its cost-cutting program, and a cyclical upturn in some of its service areas presage good earnings and dividend growth. A similar play is Phoenix-based Pinnacle West Capital Corp. Konolige expects both stocks to have one-year total returns of 20%. CMS Energy Corp. is also recovering from financial woes. But that's not why Abramson is a fan. "It is one of the more aggressive U.S. companies in making new investments in international power projects," he says. "And there's an awful lot of growth in other countries."

Clearly, with deregulation on the agenda, utilities are no longer the safe haven they once were. But for astute investors, the change may bring rewards that could be sweet indeed.

By Suzanne Woolley in New York



ELECTRIC UTILITIES HAVE TAKEN A BEATING



TAKEOVERS

IS KEMPER TRYING TO GIVE AWAY THE STORE?

The CEO seeks a quick sale. Going it alone makes better sense

By the night before Christmas, Kemper Corp. Chief Executive David B. Mathis already had his New Year's resolutions in order. At a Dec. 23 annual meeting in Chicago, Mathis set out to soothe the stockholders of the financial-services company, who were upset with his handling of takeover bids from General Electric Co. and Consec Inc.. Both bids had been abandoned, causing a sharp drop in Kemper stock.

To push the stock back up, Mathis resolved to find another buyer. Goldman, Sachs & Co., he told the sparse crowd, was already circulating the offering books to prospective buyers. "The for-sale sign," Mathis declared, "is up."

HERO TO GOAT. But should it be? Mathis' plan has all the earmarks of a fire sale: an eager seller in a weak negotiating position peddling damaged goods at an inopportune time. With financial-services companies out of favor because of rising interest rates, it's clear Kemper today can't command the \$67 per share Consec offered in June. Even the \$60 that GE floated in May would be a stretch. As of early January, analysts pegged the likely opening bid at \$50 per share. "It's a terrible time to sell it," argues Robert W. Back, an analyst at SNC Capital Management Corp. Yet momentum is building for a quick sale, with Dean Witter Discover, SunAmerica, and Bank of Montreal among the rumored interested buyers.

The best outcome for Kemper, though, might be no sale at all. Before GE came along, Mathis had just finished a broad restructuring that never had a chance to bloom. After becoming CEO in 1992, he took decisive steps to halt real-estate litigation losses that had undermined Kemper's results for years. He exited



MATHIS: *His restructuring never had a chance to bloom*

cyclical businesses that had made the company's earnings unpredictable, selling four major subsidiaries. He integrated its life-insurance operations, consolidated its money-losing broker-dealer, and positioned the mutual-fund arm for expansion. "You've got the potential for a much better company two years down the road," says analyst Ira L. Zuckerman at S.B.S. Financial Group.

Yet due to his management of the takeover maneuvering, the gentlemanly Mathis has gone from hero to goat. Initially, a defiant Mathis accused GE of

trying to "steal" a resurgent Kemper with a "lowball" \$55 bid. But after GE upped its bid to \$60, he allowed the deal to slip through his fingers. Then he embraced little-known Consec, which ended up being unable to finance the deal. "You went to bed with a company that was a dwarf against a giant. I don't call that great management," complained Hans Mueller, an investor and Milwaukee businessman, at the annual meeting.

Investors and analysts, further, gripe that top Kemper executives have the wrong incentive to sell—golden parachutes paying as much as \$19 million—and new jobs waiting in the wings. Mathis, for instance, has agreed to head Kemper's former parent—the now-independent Kemper National Insurance Cos.—once he extricates himself from his current position. That hardly inspires confidence in management. "I don't get the sense their heart is still in it," says Robert N. Gensler of T. Rowe Price Associates Inc., which sold a large Kemper stake last year. Neither Mathis nor a Kemper spokesman would comment.

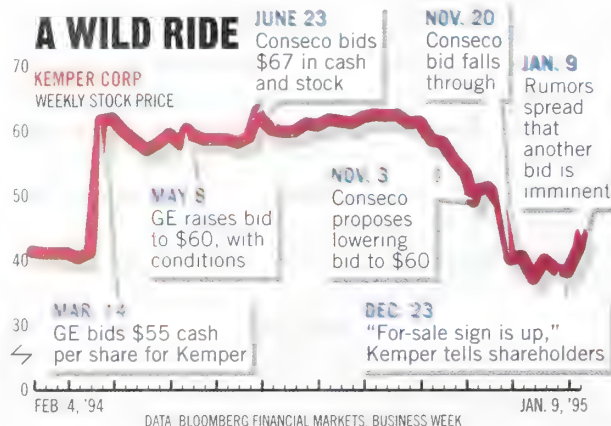
Mathis has pledged not to give away the company at "an inadequate price." And when he was battling against GE last spring, he appealed for another year of independence so Kemper could reap the benefits of its restructuring. But with antsy institutional investors pushing for an immediate payoff, he's likely to go for a quick deal.

DEFECTIONS. But maybe he should just take down the for-sale sign. To be sure, the recent turmoil has hurt, triggering broker defections at Kemper's shaky securities firm and discouraging independent brokers and financial planners from selling its mutual-fund and annuity products. But Kemper's life-insurance units are posting strong results after an investment-portfolio re-

vamp last year. And the asset-management arm, which has suffered along with most mutual-fund companies, remains a strong franchise that could benefit from consolidation in the industry.

Whatever the case, Mathis needs to put an end to the uncertainty soon—and without selling Kemper short.

By Greg Burns in Chicago



DATA: BLOOMBERG FINANCIAL MARKETS, BUSINESS WEEK

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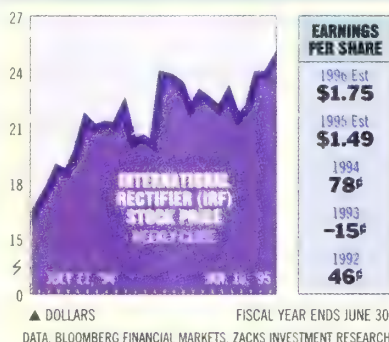
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BY GENE G. MARCIAL

OOMPH FROM 'MUSCLE CHIPS'

International Rectifier (IRF) is by no means a household name. But boy, do the big boys love this Big Board stock. Institutional investors have been snapping up the shares, driving them to 25 from 15 in July. And they say that the ride isn't over yet. One New York money manager swears that the stock is going to sizzle to 40. What's

HEADING FOR 40?



so hot about International Rectifier?

Three things: Its products have fast-growing markets worldwide. Earnings have been popping and are expected to exceed Street expectations. And Rectifier's growing links with Motorola have led pros to speculate on a takeover. In a buyout, Rectifier is estimated to be worth 45 a share.

At first glance, the company would seem to operate in the volatile semiconductor industry, since it is a major producer of "power" semiconductors. And Rectifier seems closely linked to the cyclical auto industry, because its major product is used as an electronic switch for brakes and fuel-injection systems.

In fact, Rectifier makes metal-oxide semiconductor field-effect transistors (MOSFETS), which switch or control electricity at high voltage. They serve a more diversified market than semiconductors: MOSFETS are used in cars, computers, TVs, copiers, fax machines, fluorescent lamps, and aerospace applications. So when the semiconductor industry is in a slump, demand for MOSFETS is less apt to droop.

MOSFET transistors, which Rectifier pioneered, have grown at a steady annual 24% over the past five years. As an example of their growing applica-

tions, an average car now uses 40 to 100 MOSFETS, up from fewer than 10 five years ago. Some 15% of Rectifier's MOSFETS go into autos and 25% into computers. Michael Gumport of Lehman Brothers says: "If memory chips are the brain, power transistors are the muscle chips that act on what microprocessors want to do."

Gumport has raised his earnings estimates three times this year to catch up with Rectifier's rebound: It stumbled in 1992 and 1993 from manufacturing problems. In the year ended June 30, 1994, Rectifier made 78¢ a share, vs. a 15¢ loss in 1993. In 1995, Gumport sees the net jumping to \$1.50 and to \$1.70 in 1996—more or less in line with the estimates shown in the chart.

Rectifier claims 20% of the \$2 billion power-transistor market—nearly twice as much as Motorola. Some big investors think Motorola may seek to up its share of this growing business by going after Rectifier. Early in January, the two companies signed a long-term cross-licensing agreement for patents they hold in the technologies of power MOSFETS and related products. This latest pact, some traders say, could be the first step towards a Motorola move on Rectifier. Both Rectifier and Motorola declined comment.

A BIOTECH BABY CATCHES COLD

Tiny North American Vaccine (NVX) certainly has guts. It wants to get its foot into a small field controlled by such biggies as Merck and American Cyanamid. But startup North American is waging a losing battle, says Evan Sturza, editor of *Sturza's Medical Investment Letter*.

Specifically, it's gunning to sell vaccines against common bacterial and viral diseases. Its lead product, DTaP, targets acellular pertussis—or whooping cough. The company is up against the short-sellers, who insist DTaP is less effective than the inexpensive vaccines already available. The market seems to agree: Since September, the stock has slumped from 14 to 8.

Results of the vaccine's third clinical test, according to President Sharon Mates, showed that only 4% of children receiving DTaP came down with whooping cough, compared with 14% of the control group. She points out that this represents "a reduction of 71% in the incidence of disease."

No so fast. Sturza says that this 71% reduction rate is not so good as those of other acellular and whole-cell vaccines, which have efficacy rates of 80% to 85%. North American's stock has fallen 25% just since it announced the trial results. But even at its current price, Sturza feels it is overvalued—and worth only 3. A company spokeswoman says: "We remain optimistic about our vaccine, and we'll file for Food & Drug Administration approval this quarter."

AMID THE RUBBLE, A MEXICAN GEM

Since the peso's tumble, Mexican stocks have been ferociously hammered, with many losing 40% to 80% of their value in just a few weeks. Many American investors have bailed out fast. But not all. Money manager Willie Weinstein is among the daredevils scooping up the leavings.

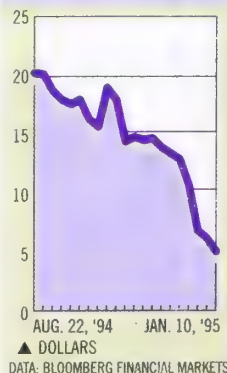
One pick is Banca Quadrum (QDRMY), a little-known financial company that converted itself into a commercial bank in November. Its shares have collapsed to 5¢, down from 20 in August. Previously called Servicios Financieros Quadrum, this Mexico City outfit provides small-to-midsize Mexican businesses with financing—usually secured by accounts receivables.

Weinstein expects the bank to remain solidly profitable. Adjusted for the sudden peso devaluation, its earnings were 80¢ a share in 1994, he figures. For 1995, Weinstein foresees 95¢ or more.

But the important thing, he says, is that Quadrum has become even more undervalued: It's trading at book value of \$5 a share—and at a depressed

multiple of five times its estimated earnings for 1995. "The company has assets of extremely high quality," he says. The balance sheet is strong, with little debt, he adds. He's convinced that the stock will head back north—to 12 in the coming year.

HAMMERED WITH THE PESO



THE 1994 BUSINESS WEEK EUROPE ROUNDTABLE OF CHIEF EXECUTIVES

Great Expectations: Europe, China, the Emerging Markets

Management didn't get smart," says Siemens Nixdorf CEO Gerhard Schulmeyer, "the old system just didn't work anymore. That's why we're changing it. The old system for most European corporations was top-down management, lifelong employment, and lavish worker entitlements – a perfect combination that handicapped them in the global race for market share.

But after three years of low or no growth, European corporations are rising from the ashes. This phoenix is a new bird – lean after painful delayering and downsizing, and predator for profits in the emerging markets of the former Soviet bloc and the developing countries of Southeast Asia.

Schulmeyer was joined by Dr. Henry Henger; Romanian President Ion Iliescu; U.S. Ambassador to NATO Robert Hunter; U.K. Minister of Trade President Michael Heseltine, MP; and more than 100 corporate chief executives of Europe's leading enterprises at the fifth-annual Business Week Europe Roundtable of Chief Executives in London, U.K.

They met to forge the new system – lean organizations, process-oriented management, outward-looking business strategies to get Europe back into the global game.

Wing Taylor

Schulmeyer says the faults of the old system were twofold. "First the speed with which things changed on the factory floor made command structures irrelevant, and people at the lower levels recognized this. Second, information moving up through the organization became so complex that managers needed decision support systems." As a result, Schulmeyer says the real issues became muddled in a cavalcade of decision makers too far removed from the business to be effective. The quality of management decisions suffered and a huge disconnect yawned between upper management and the factory floor.

"Communication technology," explains Al Ahold, **U.S. Vice-President and Member of Corporate Executive Board**, Edward Moerk,



"basically kills the management model we all grew up with, the Taylor model, which is the command model with a big guy at the top and 16 layers beneath him."

"Advances in communications technology are facilitating a fundamental change," says **eunetcom Business Development Director Neil Rafferty**. "Business can now put information in the hands of whomever needs it to make a competitive decision, anywhere in the world. And that has a direct effect on the bottom line and on management structure."

As a result, Tayloristic hierarchies have been marginalized. For example, Ahold's chain of supermarkets in the United States, which

First the speed with which things changed on the factory floor made the Tayloristic command structures irrelevant, and people at the lower levels recognized this.

have from \$20-50 million in sales, operate as totally separate enterprises. "The only thing centralized is the supply system," says Moerk. "With the right telecommunications and information technology, they run their own show so they can make their own decisions with the speed they need to remain competitive."

That kind of empowerment has made it possible for European companies to eliminate entire layers of management and cut payrolls for healthier margins. At Siemens Nixdorf, Schulmeyer cut the European workforce from 52,000 to 38,000. Then the company focused on empowering its best-in-class people with new tools and techniques.

Royal Ahold, Holland's top supermarket chain with \$15 billion in revenues, and sales and profits that are doubling every five years, is eliminating an entire level of management (5,000 employees) to get even leaner. But in the European culture, mass U.S.-style downsizings are both unfamiliar, and unwelcome.

"People are asking, 'Why? Why do we have to do it?'" says Moerk. "When you explain that there are millions of people all over the world who would love to do their jobs for one-tenth of their salary, they begin to understand."

The New Age

Hundreds of European corporations have already restructured, and embraced team-oriented, market-focused, customer-driven, flexible strategies. **Gemini Consulting Co-Chairman James Kelly** sees the transformation of the

European corporation as part of a new social contract necessitated by the advent of the "Communication Age."

"The message is not just about making profits, saving costs, and cutting people," Kelly observes, "It's about releasing the imaginations, energies, and the spirits of people to contribute to their organizations and to society in totally new ways, ways not previously possible in our industrial organizations."

Minolta Europe GmbH Director

Akio Miyabayashi says that the communication age places a premium on creativity, and that necessitates a human-centered corporate environment that is led by managers who have more in common with coaches and cheerleaders than with dictators. "The marketplace is too complex for the leaders to do the thinking for

everyone, and workers today want to do the thinking themselves."

"The bottom line," says Moerk, "is that most organizations of the future will be based on the concept that people want to contribute, they want satisfaction, they want to run things."

Miyabayashi calls this heightened awareness of employee fulfillment an emphasis on "humanware." The premise is that without employee satisfaction, corporations cannot deliver customer satisfaction, making "humanware" as vital to success in the communication age as hardware and software.

"The human element will be the core of everything in the future," says Miyabayashi. "We create products to give pleasure and happiness to their owners and users. If a company wants to create a product that people will want, will enjoy owning, and will get excited about using, they must create an environment in which their staff gets happiness and enjoyment out of what they do."

Tailor-Made Success

Human-centered, customer-focused, flat, global. Benetton, the \$613,000,000 international outfitter, epitomizes the new model for successful European companies. Founded in Italy 30 years ago, the company has maintained the creative, entrepreneurial culture of a start-up by remaining focused on the core aspects of the business and outsourcing everything else. Now it's ubiquitous – 7,000 stores in 120 countries.

Benetton Chief Financial Officer Marco Polo credits capital efficiency with the company's success. With only \$1 billion total capital invested, 5,500 employees, and 196 managers, the company's annual revenues are more than \$2 billion.

"Not being burdened down by brick and mortar and thousands and thousands of people has kept us flexible," says Polo. "The Benetton stores are independently owned; Benetton owns only the 30% of the production required to maintain quality, and produces one collection worldwide." Moreover, \$600,000 per year invested in technology enables the company to keep labor costs low and efficiency high. Benetton's only warehouse – the technologically sophisticated "Big Charlie" – is so efficient, it ships to all 7,000 stores directly and takes only 12 people to operate.

"If people stopped wearing clothes," says Polo, "we have an organization that is smart enough and flexible enough to start producing umbrellas in many different colors tomorrow."



"Advances in communications technology are facilitating a fundamental change upon business. Business can now put information in the hands of whomever needs it to make a competitive decision, anywhere in the world. And that has a direct effect on the bottom line and on management structure."

*eunetcom Business Development
Director Neil Rafferty*



er There

With European companies like Benetton, Royal Ahold, and Siemens Nixdorf down to their fighting weight, they're the prowl, poised to regain market share beyond the boundaries of Western Europe. While the emerging markets of the former Soviet bloc, China, and Southeast Asia raise new growth opportunities, they also present a host of formidable competitors for producing goods and services. "In the U. K. it costs on average £50 per day to employ a worker; in Singapore, it costs £25 per day," says **Grand Metropolitan Plc. Chairman Lord Sheppard**. "We are simply not competitive enough."

Lord Sheppard calls for a new partnership between European corporate leaders and governments to liberate business from over-

regulation, take steps to lower the cost of labor to competitive levels by capping worker benefits, and eliminate the costly and cumbersome bureaucracies that hinder entrepreneurial startups.

"We need to come together to find new ways to grow wealth," says Lord Sheppard. "The message from the emerging markets to each of us is wake up; the world doesn't owe us anything; the continent doesn't owe us a living."

U.K. Board of Trade President Michael Heseltine has identified a power shift from national governments

multinational corporations. "Nation-states are competing for the investments of corporations," says Heseltine. "Governments must now look at multinational corporations as customers, and we must provide them with what they want or lose their investment."

ing East

What they want is skilled labor, at low wages, in expanding consumer markets. They need look no further than the East's back door, where the demise of communism has opened up a vast new consumer

market connected historically and culturally to Western Europe and clamoring for quality goods and services.

According to **Coca-Cola Company's Northeast Europe/Middle East Group senior vice-president E. Neville Isdell**, the payback is more than profits. "With \$1.5 billion in capital and strategic partnerships involving local and international bottling partners," says Isdell, "we have quickly gained soft-drink leadership throughout Eastern Europe."

But even more important to Romania, Poland, and Russia, Coca-Cola has become the major driver of the "multiplier effect," generating local jobs, know-how and business opportunities, and nurturing an entrepreneurial culture that will prove critical to the overall development of stable, market-oriented economies.

GE Lighting Europe CEO Charles Pieper identifies the same phenomenon resulting from the company's 1990 acquisition of Tungsram, Hungary's largest lighting company. "It's not just a financial issue," says Pieper. "We have 800 engineers in lighting worldwide, 400 of them in Europe, 350 of them in Hungary. It's more than a new market, it's a place to develop talent." The Tungsram operation now holds "centers-of-excellence" status for GE lighting operations worldwide in basic research in glass, compact fluorescent lamps, and other new technologies. Under GE, Tungsram has contributed close to 50% of Hungary's export growth to the United States over the past two years.

Romanian President Ion Iliescu says there are many more Tungsram-style success stories waiting to be told in Eastern Europe. But Romania's transition to a market economy has been slow compared to the Czech Republic and Hungary.

"Unlike Poland, Hungary, and the Czech Republic," says President Iliescu, "Romania had no debt when it emerged from its revolution in 1989. But that also meant that we had no relationships with Western banks, no credit history to serve as a precedent for new loans. So the banks ignored us."

But Iliescu says the doors are wide open to Western investment. "Romania has committed itself to the privatization of 6,700 state-owned enterprises. With 700 privatized over the last two years, thousands of opportunities remain for Western European investment in Romania."



"The message is not just about making profits, saving costs, and cutting people. It's about releasing the imaginations, energies, the spirits of people to contribute to their organizations and to society in totally new ways, ways not previously possible in our industrial organizations."

*Gemini Consulting Co-Chairman
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Heseltine



All Aboard the Orient Express

Further east, European companies are finding a market even more vast – 900 million consumers in an arc that stretches from Japan, along coastal China, and southward to Southeast Asia. There the growth rates are higher, the markets are larger, and the entrepreneurialism is palpable.

Sophia University Professor and Gemini Consulting, Japan, Chairman Dr. James Abegglen says that European investment in the region is lagging behind that of Japanese and American investors, particularly in such key emerging economies as Indonesia and Malaysia. "The center of world industry has shifted to East Asia," Abegglen says. "There must be a parallel shift in Western management attention and understanding."

Critical to that understanding is a Japan strategy. Japan comprises about two-thirds of the total economy of the area – it is the main supplier of capital and technology to the rest of the region. "As the region moves to a greater integration of trade and investment," says Abegglen, "a Japan strategy is an essential part of a total East Asian strategy."

GE Lighting Europe's Pieper, who was formerly CEO of GE Japan and GE Medical Systems, Asia, says there are three reasons to anchor an Asia strategy in Japan: resources for the entire region are most efficiently allocated from there; the competition

is typically Japanese and can be better observed and understood from a Japanese base; and the technology flow from Japan is more relevant to the emerging Asian markets than from the U.S.

"For the Asian market," says Pieper, "we often take technologies from the U.S. and 'Japanize' them take out 20% of the features and 50% of the costs through redesign. Fewer features, lower costs, and less design is what sells in that marketplace, and we're already producing it for Japan."

But just as important as a Japan strategy to marshalling growth in Asia, Abegglen advises that European corporations invest in local talent. "European companies active in Asia must staff Asians in their Asian operations. Asian employees will bring with them their networks of Asian connections that are so critical for Europeans trying to do business in the region."

"We're finding the benefits in Asia are not just access to markets," says Pieper. "In Asia the products and people are making our busi-

nesses more successful everywhere else. Our whole business is changing because of our participation there."



Henry Kissinger



Robert Hunter

Whither NATO?

"The American people have expended more blood and treasure in the defense of Europe than in any other endeavor other than the Civil War." In the absence of an evil empire to provide a *raison d'être*, **U.S. Ambassador to NATO Robert Hunter** is trying to justify NATO's existence. So NATO is expanding eastward under two new strategies: the Evolutionary Approach to expansion, under which NATO will admit new, full members, and the Partnership for Peace, which is designed to prepare potential NATO members for full membership if they qualify.

"If history is kind and we are successful," says Hunter, "we can see an extension eastward of the European Civil Space. But if history is unkind, NATO will have lost no time and no effort in providing for more robust allies to play a full role in the security of the continent."

But how far eastward and under what criteria? "I have the most serious questions about the concept of the Partnership for Peace," says Dr. Henry Kissinger, chairman of Kissinger Associates, Inc. and former Secretary of State. "I believe this will lead, in the long run, to a watering down of NATO. There needs to be a line drawn against which it is clear who belongs to what and then to ease whatever tensions exist across that line, but in my mind that should be done not by NATO but by the European Security Council."

Even the nuances of the debate are enough to raise the ire of the Warsaw Pact-less Russia. In the United States, the growing debate is unfolding along partisan lines, in violation of a post-war taboo concerning matters related to European security. Whatever the outcome, 'Whither NATO?' will be the most serious European security issues from Vancouver to Vladivostok.

Martin A. Keohan is a New York-based business writer.



"Romania has committed itself to the privatization of 6,700 state-owned enterprises. With 700 privatized over the last two years, thousands of opportunities remain for Western European investment in Romania."

Ion Iliescu, President of Romania



DOCTORS WITH UNION CARDS

Private physicians join up to do battle with big insurers

After Disa Sacks hung out her shingle in 1992, the 32-year-old dermatologist found that she couldn't survive without signing on to insurance companies' physician networks. Sacks resented the interference in her medical judgment by the networks, which cap doctors' fees and control the tests and operations they prescribe. In December, Sacks, who practices in Rockledge, Fla., figured so fed up that she took a drastic step: She joined a union.

The union, the Tallahassee-based Federation of Physicians & Dentists, has signed up 500 private practitioners in Florida. So far, it's only adding members on the contracts that insurance networks offer them. The next step is to negotiate with insurers for each doctor individually, then eventually for all of them as a group. Sacks and her colleagues aren't yet ready to trade their white coats for blue collars and picket signs. But they hope that collective strength will give doctors the clout to negotiate on a more equal basis with the insurance companies and Prudentials of the world. "We haven't found out how to harness" the power of private doctors, says Sacks. "That's what this organization is for us."

If the federation succeeds, it could change up doctors' traditional role as solo practitioners. Some 75% of the country's 100,000 private practitioners have signed contracts with managed-care networks, according to the American Medical Assn. Currently, most deal individually with these insurance companies. Now many doctors are joining the Florida group closely. If they pull it off, "I'd be interested in seeing what they do," says Gary Robinson, the executive administrator of a California doctors' union, the Union of American Physicians & Dentists (UAPD), which also has private-practice members but doesn't bargain for them.



SACKS WANTS TO HARNESS DOCTOR POWER

The Florida federation's biggest problem is the Sherman Antitrust Act. The union was formed in 1988 as part of the National Union of Hospital & Health Care Employees to represent doctors at state hospitals. There's no antitrust problem with these 600 members, who work for an employer. But private practitioners are self-employed business owners. If they jointly negotiate fees, the Federal Trade Commission

WHY DOCTORS WANT TO UNIONIZE

Private practitioners in Florida want more clout with insurer-run doctor networks over issues such as:

- FEES** How much doctors will be paid for each procedure or test
- MEDICAL JUDGMENT** When tests and operations are appropriate
- BILLING** Quantity of paperwork and how fast doctors must do it
- MEMBERSHIP** Reasons doctors can be removed from a network

sion may accuse them of illegal price-fixing. That's what happened in the late 1980s to the Colorado Union of Physicians & Surgeons, which disbanded.

Last year, the FTC tried to clarify the issue in talks with the AMA. It issued guidelines saying that to avoid market domination, no more than 30% of specialists in a city can join forces. They also must share "significant financial risk." Otherwise, "collective bargaining among independent physicians is illegal," says an FTC official.

MASTER DEAL. Robinson's union, based in Oakland, Calif., has worked within the guidelines. His group, which represents 5,000 public-sector staff doctors, also formed a nonprofit joint venture for 650 of its private practitioners. The venture negotiates fees with insurance companies and distributes the payments to doctors according to the work they perform.

The Florida federation doesn't want to go to such lengths. Jack Seddon, its executive director, says his union should be able to negotiate a master contract to set minimum fees and other conditions for private practitioners. Each doctor then would sign a separate deal with an insurance network, much as football players sign individual contracts governed by a labor agreement between the players' union and the football league. The federation has hired an antitrust lawyer and a labor lawyer to help make its case in Washington. Meanwhile, the organization is helping members individually. "We're not looking for a fight," said Seddon.

Still, he's likely to find one if the federation tries real bargaining. Andrew Crooks, the head of Prudential Insurance Co.'s Orlando health care unit, says if doctors don't like network restrictions, they shouldn't join. Managed care works only "if you have like-minded physicians willing to work together," he says. Federation members worry that insurers may retaliate by cutting them out of a network.

Whether the Florida doctors' union takes off or not, "the days of the Lone Ranger have ended," says UAPD President Robert L. Weinmann. One way or another, doctors are likely to start banding together.

By Peter Valdez-Dapena in Miami, with bureau reports

EDITED BY AMY DUNKIN

AFTER THE FIRE IN EMERGING MARKETS

Anyone who invested in emerging markets last year without understanding the risks must have learned a lesson by now. In a few short weeks, Mexico's *bolsa* declined about 42% in dollar terms following the sudden devaluation of the peso. Asian markets that sizzled in 1993 slumped in 1994. Hong Kong fell 31%, Malaysia 20%, and Thailand 18% in dollar terms, says Baring Securities. Emerging-market mutual funds, often heavily weighted in Mexican stocks, plunged an average of 8.3% from Dec. 20, 1994, to Jan. 6, 1995, and declined 12.8% last year, according to Morningstar Inc.

Do you feel like turning tail and heading home? Or are you patting yourself on the back for never plunging part of your savings into emerging markets in the first place? Well, neither is the appropriate response.

Emerging-market stocks should play a role in all but the most conservative portfolios, investment pros say. As with many developing coun-

tries in Latin America, the Pacific Rim, and Eastern Europe have sometimes enjoyed triple-digit returns in a single year, they can also fall on bad news just as quickly as they rise. Coups, assassinations, currency devaluations—"those are things you expect to happen," says Michael Hoffman, manager of the Robertson Stephens Emerging Markets Fund. Indeed, 1995 may have more than its share of political and economic crises. In addition to tensions in Mexico, Russia, China, and the Middle East, a global rise in interest rates, triggered by U.S. rate hikes, will slow growth and continue to create disappointments in equity markets. These declines may prove to be excellent buying opportunities for people with the cash—and the nerve—to invest.

The danger is that investors—including U.S. mu-

AMG Data Services in Arcata, Calif. But if investors eventually see reason to flee in droves, fund managers could be forced to sell off their holdings to meet redemptions. In these illiquid markets, those losses could be the most punishing of all.

That's why emerging-market guru Mark Mobius, who

Argentina, Hong Kong, Indonesia, Mexico, and Turkey—all cited as trouble spots by other managers. "We need to know where the outlook is bad," he says. "Chances are those are the places we should be investing."

UNCERTAINTY. Managers agree it is best to buy on adversity in emerging markets. But the pros differ over whether the worst is over. For example, there's little consensus about Mexico's future. "Steer clear of Mexico," says Nigel Reidel, James Capel's emerging market strategist. Growth will slow, interest rates will remain high, and political uncertainty will continue, he says. But Hoffman counters that this is a good time to start picking up Mexican stocks. He recently purchased conglomerate Grupo Carso and construction company Grupo Tribasa, two issues he believes were overbattered, for his fund.

INVESTING Is the worst over yet?
It depends on which pro you believe,
so proceed with extreme caution

tries, the economies of Malaysia, Thailand, and South Korea are projected to grow at a 5% to 10% rate—two to three times faster than the developed world's. Over the long term, this should translate into dramatic gains for their stock markets.

But these markets are extremely volatile. While coun-

tual-fund shareholders—who flooded into these markets in recent years, often paying a high price, could be easily disappointed by downturns. After a flurry of redemptions when the peso was allowed to float on Dec. 20, mutual-fund companies saw inflows to their Latin America funds the first week in January, according to

manages several funds for the Franklin Templeton families, is keeping as much as 30% of his portfolio in cash while he searches for "realistic and sustainable" stock prices. Both professional and individual investors have to "look for value and not chase short-term performance," he warns. Mobius currently sees values in



for the rest of Latin America, some managers see parallels with Mexico in Argentina, which is also very dependent on foreign capital. However, Argentina has a lot of domestic financing

while India may be unsettled through its March elections, Cornell figures it should have a good year after that.

Most managers aren't ready to dip into Eastern Europe and former communist-bloc countries. But the conventional assessment of the politi-



is generally a favorite. Argentina and Brazil, two countries that turned in strong performances in 1994, have fueled speculation about prospects for 1995, since some managers believe they are now overvalued. Last year dashed investor hopes that Asia would turn in better performance like 1993, but the average total return on Pacific stock funds was down and several funds retreated more than 70%. In Asia, rising rates wreaked havoc on Hong Kong property prices while China's fledgling market cooled as cracks deepened in the country's relationship with the West. For these reasons, some investors are avoiding these core emerging markets. Joyce Cornell, an emerging-markets portfolio manager at Scudder, Stevens & Clark, thinks peripheral markets such as Indonesia and the Philippines are more interesting. And

cal systems as unstable is overblown, says Suzanne Patrick, who covers Eastern and Central Europe for Arnhold & S. Bleichroeder Inc. Poland is the economic powerhouse of the region. "When you get to '96 and '97, this is the story," she says, although she doesn't expect to see much growth in '95. Czech and Slovak Republics, Hungary, and the Baltic states are still undergoing economic transformation and are growth stories for the future.

RUNNING THE RISK. Russia attracted some investor attention early in 1994, but fighting in Chechnya, not to mention severe economic problems, has squelched interest. "I wouldn't touch Russia with a 10-foot pole," says Scudder's Cornell.

Africa and the Middle East still don't seem ready for big-time investing, either. But a few "pre-emerging" countries there are generating interest. Cornell likes some mining stocks in Zimbabwe and oil

stocks in Oman. Markets in Israel and South Africa are far more sophisticated than their neighbors but are risky for 1995. Israel's market hinges on the success of the Arab-Israeli peace plan. South Africa, formerly an investment pariah, should get a boost when it is included in the International Finance Corporation Emerging Market Index this year. Fund managers will buy up South African equities to match the index's country weightings, says Rendell.

If you have a long-term time horizon and a taste for risk, you should invest up to 30% of your equity holdings in emerging markets, says Mobius. For most people, buying a mutual fund that offers a diversified basket of emerging-market securities makes the most sense. Montgomery Emerging Markets is the top pick of Jay Schabacker, editor of *Mutual Fund Investing*. He also recommends Fidelity Emerging Markets and Lexington Worldwide Emerging Markets.

You can make a bet on a region by choosing a fund that focuses on Latin America or Pacific Rim countries. Or you can pick a closed-end single country fund. Many are trading at huge discounts to their underlying holdings, which could make them good values if you like to gamble. The Thai Fund is at a 20% discount to its net asset value; Scudder New Asia is at a 17% discount.

Finally, you can choose from hundreds of American Depositary Receipts, which trade in dollars on U.S. exchanges but represent shares in foreign companies. This way, you can invest in companies or sectors you're interested in. But while infrastructure, telecommunications, bottling, mining, retail, and banking are compelling themes to explore in emerging markets, the performance of individual issues is often linked to the local market as a whole.

No matter what strategy you choose, 1995 may be a tough year for emerging markets. But the rockier it gets, the more opportunities there will be to snap up bargains in the world's fastest-growing nations. *Amey Stone*

Mapping the Emerging Markets' Investment Landscape

LATIN AMERICA Selected stock markets could bounce back, although money managers disagree about which are the best bets. Many are avoiding Mexico. Peru and Chile are favored, while Argentina and Brazil could face the same problems as Mexico.

ASIA/PACIFIC Look out for interest-rate shock in Hong Kong, China, and Malaysia. Managers like peripheral markets, such as Korea, Indonesia, and the Philippines. India is showing good growth and stocks should perform well after March elections.

AFRICA AND THE MIDDLE EAST Money managers are intrigued, but for most it's too early to step to the plate. The pros are watching Egypt, Oman, Morocco, Botswana, and Zimbabwe. South Africa and Israel are more developed but tricky politically.

EASTERN EUROPE Market watchers say 1996 and 1997 will be strong years for the region. As the economic powerhouse, Poland merits attention, and the Czech and Slovak Republics are promising.

HOW FREQUENT FLIERS CAN BEAT THE CLOCK

Most people's pre-Christmas frenzy centers on shopping. But Martha Lindeman, vice-president at Playboy Enterprises in Chicago, spent the holiday searching for ways to maximize her family's payoff from more than 200,000 frequent-flier miles. Scrambling to beat Feb. 1 and Apr. 1 hikes in mileage requirements for domestic and international coach travel, respectively, Lindeman and her husband redeemed enough miles for three free tickets to Salt Lake City and four to Paris. "When I placed the call, I didn't even know where or on what dates I wanted to travel," she says. "I just knew I wanted to cash in at the lower mileage levels."

Like Lindeman, millions of frequent fliers are hustling to beat deadlines that will generally boost mileage needed for mainland U.S. travel by 25%, or 5,000 miles, and hike requirements for such popular destinations as Hawaii and Europe by up to 50%. That's no paltry jump: An added 5,000 miles can mean 10 extra flights to earn a free ticket. And by late spring, the largest U.S. carriers will have "use-it-or-lose-it" restrictions on how long miles remain valid, making it even tougher for occasional fliers to reach award thresholds.

DEVALUED. "In recent years, airlines have changed their programs to look more alike, making airline mileage into a common currency—and now that currency is being devalued," says business-travel author Christopher McGinnis.

If you need miles to beat the Feb. 1 deadline, your options are limited. Members of the American Express Mem-

bership Miles program, which gives one mile for each dollar charged on the AmEx card, can transfer mileage to their accounts at six carriers, including Continental Airlines and USAir, in as little as a week—perfect for topping off an account. And Continental will sell you up to 20% of the miles

to use a rental car or hotel room in conjunction with a trip, be sure to book with one of your airline's partners. Large ones, such as Hertz, get high marks for posting bonus mileage quickly.

If you're within shouting distance of an award, it may be worthwhile to take a trip pronto just to nab miles. Pick a route with rock-bottom fares. American, for example, flies between Los Angeles and San Diego for just \$71 round trip, while United shuttles between Chicago and Detroit

increased until April, you can be a bit more creative in your mileage-accumulation tactics. For instance, carrier such as USAir give as much as 2,500 miles to member who apply for—and quickly use—the bank credit card the airlines sponsor. Diner's

FLYING

Club has a similar come-on. MCI Communications is offering up to 2,000 miles to customers who switch to its long-distance service. And dining-for-mile plans at Northwest and American give mileage based on the tab at participating restaurants.

MIX AND MATCH. You should also investigate switching miles from other travel programs. Besides AmEx Membership Miles plan and Diners Club's Club Rewards program, Hilton Hotel HHonors Reward Exchange lets members transfer points from Hilton's frequent-sleeper program into mileage on Alaska Airlines, American West, Delta, or United. Hilton's conversion rate—10,000 hotel points become just 1,500 airline miles—is a bargain. But it could do the trick if you're a few thousand miles short. Be careful, though: Mileage from unusual promotions or even credit card charges can take as long as 60 days to show up in your account.

If you're redeeming on American or USAir, ask for an award certificate, which can be held up to a year before you need to exchange it for a ticket. Then you have another year to actually fly. Even if your carrier only redeems mileage directly for tickets, you can always change the date or destination later—as long as you complete your travel within one year.

Whatever you do, you must cash your miles in before the changes take effect. That means the last date to beat the hikes isn't Feb. 1—it's Jan. 31. To be safe, forget the mail; most carriers now accept redemption requests by phone. So act fast—you'll be grounded. *Jim Ellis*



CHANGE

Required mileage for one free domestic coach ticket increases 25%, to 25,000 miles, on American, Continental, Northwest*, and United

Required mileage for free coach travel to Hawaii, the Caribbean, Europe, and Asia jumps 17%-50% on United, American, Northwest,* and Continental

Required mileage for one free domestic coach ticket on Delta falls 17%, to 25,000 miles, but minimum mileage credit given for each flight is cut 50%, to 500 miles

Minimum mileage drops 33%, to 500 miles, on USAir, and mileage for free travel to Caribbean and Mexican destinations increases 17%, to 35,000 miles

* EXCEPT FOR LIMITED OFF-PEAK PERIODS

EFFECTIVE DATE

FEB. 1

APR. 1

MAY 1

MAY 1

DATA: AIRLINES, BW

needed for an award at a cost of \$25 per 1,000 miles.

But your surest bet is to fly—fast. Airlines normally give mileage credit within five business days of the flight. So if you've got trips that can be moved up to even Jan. 25, your mileage should post in time to beat the changes. And if you plan

for \$68 round trip. Either jaunt earns a quick 1,000 miles. "A \$68 ticket may be worth the 5,000 miles you're going to save by redeeming at the lower level," notes Randy Petersen, publisher of *InsideFlyer* newsletter.

If you're shooting for international awards to Mexico or Asia, which won't be

in the Internal Revenue Service is new regulations governing partnerships. Last spring, accountants went ballistic. The regulations, which described abusive partnerships, were so strict that almost anyone could violate them without getting it and lose their assets at the whim of a tax commissioner, CPAs said. "To a couple of flies, they're stomping on every-thing," says Mike Lux, a partner at Deloitte & Touche in Washington. Just as the Year was about to toll, the IRS rushed out more

rules—but the complex guidelines are still

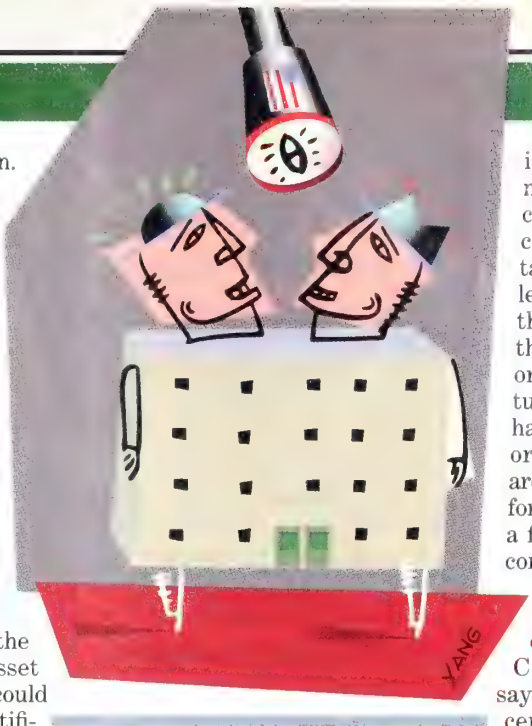
The new rules require you to form a partnership for business purposes and not to avoid taxes. But the IRS recognizes that tax benefits often arise from legitimate business partnerships, so that's O.K. For example, a family limited partnership is fine if, say, a husband and wife form it to hold an "income-producing" asset, such as an investment pool in a family business, says Jerrold L. Millford, a partner at Grant & Thornton. One of the new rules says that limited partners could not make minority distrib-

utions to the children. This provides a double tax break. The children, because they own minority interests in a business and have no say over operations, get a tax discount. And the parents remove the property from their estate. However, a partnership formed to hold the family's vacation home is a violation, and the IRS could dissolve it.

The IRS also put the kibosh on certain asset manipulations that could be used to create artificial tax losses. Previously, if you had property A that lost value and you transferred it to a partnership, you could "exchange" it for another property, B, that didn't have a loss. When you sold B, you

were able to claim the loss you incurred on A. The partnership could also claim the loss because it still owned property A. Hence, you doubled the loss.

NO TEMPS. Also disallowed is taking on a temporary partner solely to create a tax transaction, says Joe Unger, a tax partner at M.R. Weiser in New York. That might involve bringing in a foreign partner who is not liable for U.S. taxes and transferring a taxable gain in the partnership to him when the partnership buys him out. That leaves an asset diminished in value that



Under the IRS's recently revised rules on partnerships, some practices are now certain to raise the tax man's eyebrows, experts say:

- ▶ Forming a family limited partnership to hold property, such as a vacation home, which isn't "income-producing" and "actively managed."
- ▶ Transferring devalued assets to a partnership so that both you and the partnership can claim the same tax loss separately.
- ▶ Transferring a taxable gain to a temporary foreign partner not liable for U.S. taxes—thereby creating a loss for the U.S. partnership.

the partnership can claim as a loss.

It's also considered abusive when two corporations form a partnership and the new entity purchases stock in another company that pays a large dividend. Normally, the investing corporation could exclude 70% of the dividend from taxes in exchange for reducing how much the partnership paid for the stock. That increases the company's profit—and taxes—when it sells the stock. Companies formerly could use a partnership to avoid having to reduce the basis.

The new rules also spell out allowable strategies. For

instance, many business owners prefer S corporation status because they're only taxed on the individual level—and not also at the corporate level, as they would be with an ordinary C corp structure. But S corps can't have foreign investors or owners. To get around this, S corps can form a partnership with a foreigner to house the company's assets—thus keeping the S status but avoiding the double taxation of a C corp. The IRS now says this strategy is acceptable because it's used for business reasons, such as raising capital in foreign markets, explains Richard Smith, a partner at KPMG Peat Marwick.

GRAY AREAS. Also permitted are UPREITS—umbrella partnership real estate investment trusts—which allow developers to raise capital through REITs and avoid paying certain taxes. Corporate rules require developers to pay taxes on appreciated property transferred to a REIT. But by forming a partnership with the REIT, or an UPREIT, developers can avoid taxes until they cash out. "This is

very important to the real estate industry because they've raised over \$16 billion in initial public offerings, and 73% of that was raised through UPREITS," says Smith.

The new rules are a relief to most CPAs. For one thing, now an agent, before taking action, must clear it with IRS tax experts specializing in partnership law and the pertinent industry. Still, Grant & Thornton partner Tom Ochenschlager thinks much uncertainty remains. The law is clearer, he says, but gray areas remain where one could still overstep it unknowingly.

Pam Black

BEST INFLATION. Expect personal-computer prices to fall along with phone rates. So states Standard & Poor's in its 1995 consumer price inflation outlook. —a unit of McGraw-Hill, which also owns BUSINESS WEEK—says people won't pay much more to eat out, and most other prices should remain stable. But the cost of heating with natural gas will jump 4.5%. Overall, S&P forecasts a 3% rise in the CPI.

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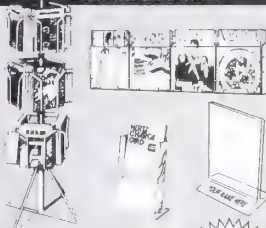
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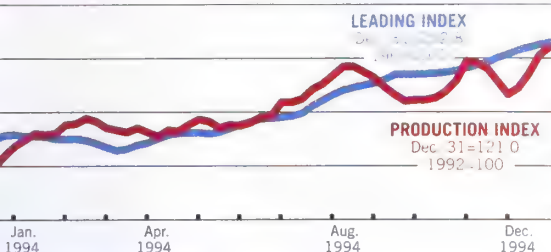
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Business Week Index

PRODUCTION AND LEADING INDEXES

Change from last week: 0.7%
Change from last year: 9.1%

Change from last week: 0.7%
Change from last year: 7.2%



Production index rose for the week ended Dec. 31, although before calculation of the four-week moving average, the index slipped to 120.8, from 121.5. For December, the index increased to 119.2 from 118.5 in November. Leading index also edged up for the latest week. The unaveraged index inched to 253.5, from a revised 252.9. The December index stood at 252.7, from November's reading of 250.2.

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LEADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (1/6) S&P 500	460.21	460.94	-1.5
CORPORATE BOND YIELD, Aaa (1/6)	8.51%	8.43%	21.4
INDUSTRIAL MATERIALS PRICES (1/6)	112.7	112.8	NA*
BANKRUPTCY FAILURES (12/30)	278	267	3.3
REAL ESTATE LOANS (12/28) billions	\$456.6	\$456.9r	8.4
VEHICLE SUPPLY, M2 (12/26) billions	\$3,571.2	\$3,558.6r	1.1
REAL ESTATE CLAIMS, UNEMPLOYMENT (12/24) thous.	321	325	9.6

Sources: Center for International Business Cycle Research (CIBC), Standard & Poor's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures of companies), Federal Reserve, Labor Dept. CIBC seasonally adjusts data on bankruptcies and real estate loans. *Historical data available from CIBC

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
MUTUAL FUNDS (1/10)	5.44%	5.98%	2.98%
COMMERCIAL PAPER (1/11) 3-month	6.18	6.32	3.18
CERTIFICATES OF DEPOSIT (1/11) 3-month	6.18	6.38	3.13
FIXED RATE MORTGAGE (1/6) 30-year	9.39	9.35r	7.30
ADJUSTABLE RATE MORTGAGE (1/6) one-year	6.85	6.78r	4.28
LIBOR (1/11)	8.50	8.50	6.00

Sources: Federal Reserve, HSH Associates, Reuters Holdings PLC

Data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

INDUSTRIAL PRODUCTION

Monday, Jan. 17, 9:15 a.m. ► Output at factories, mines, and utilities likely rose in December, the same solid gain seen in October and November. That's the forecast of economists surveyed by McGraw-Hill, a division of McGraw-Hill. The increase is suggested by new factory orders and the long workweek in December. Output rising, the average capacity-utilization rate for all industry likely edged up 1% from 84.7% in November.

BUSINESS INVENTORIES

Tuesday, Jan. 18, 10 a.m. ► Inventories of manufacturers, wholesalers, and retailers probably grew by about 0.3% in

November. Factories have already reported a 0.5% rise in their November stock levels, but strong retail sales likely drew down inventories at the store level. In October, total business inventories rose by 0.4%. Business sales likely increased by a large 2% in November, after advancing just 0.2% in October. Factory shipments and retail sales were strong in November.

INTERNATIONAL TRADE

Thursday, Jan. 19, 8:30 a.m. ► The MMS forecast is that the trade deficit for goods and services narrowed slightly, to \$9.8 billion in November, from \$10.1 billion in October. Exports are expected to increase after falling for two consecutive months.

Imports, up 0.6% in October, probably were little changed in November. The foreign trade sector was a drag on economic growth in 1994, but faster-growing exports, along with slower domestic demand, should change the trade picture this year.

HOUSING STARTS

Friday, Jan. 20, 8:30 a.m. ► Housing starts likely fell to an annual rate of 1.48 million in December, projects the MMS survey. New-home sales dropped in November, leaving builders with an increased number of unsold units. In November, unusually warm weather helped to push starts up by 6.9%. With mortgage rates rising, homebuilding should taper off in 1995.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (1/7) thous. of net tons	1,985	1,992r	5.0
AUTOS (1/7) units	115,734	0	-10.4
TRUCKS (1/7) units	88,425	0	-21.3
ELECTRIC POWER (1/7) millions of kilowatt-hrs.	NA	55,717#	NA
CRUDE-OIL REFINING (1/7) thous. of bbl./day	14,336	14,198#	7.5
COAL (12/31) thous. of net tons	16,047#	20,345	9.5
PAPERBOARD (12/31) thous. of tons	NA	905.0	NA
PAPER (12/31) thous. of tons	NA	828.0	NA
LUMBER (12/31) millions of ft.	308.9#	377.6	-9.8
RAIL FREIGHT (12/31) billions of ton-miles	19.3#	23.7	14.2

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPAA¹, SFPA², Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (1/11) \$/troy oz.	375.600	375.600	-2.8
STEEL SCRAP (1/10) #1 heavy, \$/ton	144.00	144.00	2.9
COPPER (1/7) ¢/lb.	139.9	142.4	64.8
ALUMINUM (1/7) ¢/lb.	96.5	94.0	79.4
COTTON (1/7) strict low middling 1-1/16 in., ¢/lb.	86.12	86.32	35.3
OIL (1/10) \$/bbl.	17.42	17.43	21.4

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (1/11)	99.88	101.21	111.27
GERMAN MARK (1/11)	1.54	1.56	1.75
BRITISH POUND (1/11)	1.56	1.56	1.49
FRENCH FRANC (1/11)	5.30	5.37	5.94
ITALIAN LIRA (1/11)	1624.0	1626.5	1706.0
CANADIAN DOLLAR (1/11)	1.41	1.41	1.32
MEXICAN PESO (1/11)	5.725	5.410	3.103

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

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A Guy Who's Had
The Same Job
For 50 Years,
Has Never Called
In Sick Or
Showed Up Late,
Never Taken A
Vacation Or A
Holiday, Never
Asked For A
Raise Or Griped
About His Bonus
And, Believe It Or
Not, Has No
Plans For
Retirement?



Thanks.

Remember - only you can prevent forest fires.

Index to Companies

This index gives the starting page for a story or feature with a significant reference to a company. Most subsidiaries are indexed under their own names. Companies listed only in tables are not included.

A

Arthur D. Little 58
Alaska Airlines 104
Alex. Brown & Sons 76
Alliance Capital Management 54
Altair Computing 86
America West 104
American Airlines 104
American Cyanamid 96
American Express 104
Apple Computer 13, 44, 76
Arnhold & S. Bleichroeder 102
AST Research 76
AT&T 13, 22
Atlantic Recording 48
Avid Technology 6

B

Bain 76
Banca Quadrum 96
Bank of Montreal 94
Baring Securities 102
Bates Worldwide 46
Bayer 70
BBDO Worldwide 46
Biomera 70
Biopharm 70
Boeing 86
Borden 50
Borland 50
Bridgestone/Firestone 50
British Airways 46
British Petroleum 83
Broadview Associates 44
Brown Brothers Harriman 72

C

Campbell Mithun Esty 46
Campbell Soup 46
Canon 72
Castle Rock Entertainment 79
Cemex 58
Centor Energy 93
CFE 59
Charter Investment Group 90
Chatterjee Group 90
Chem Systems 83
Chevron 88
Chicago Bears 6
Citizens Utilities 34
C.J. Lawrence/Deutsche Bank Securities 50
Cleveland Browns 6
CMS Energy 93
CNN 79
Color Tile 88
Columbia Pictures 79
Compaq Computer 13, 22, 76, 112
Computer Intelligence InfoCorp 76
Comsat 87
Conseco 94
Continental Airlines 104
Continental Bank 34
CS First Boston 54

D

De-Sta-Co 92
Dean Witter 44, 94
Dell Computer 76
Deloitte & Touche 105
Delta Air Lines 104
Denny's 88
Deutsche Telekom 6

Digital Equipment 76

Dillard Department Stores 48
Diners Club 104
Dover 92
Dow Chemical 83
Dreyfus 50
DRI/McGraw-Hill 82
DuPont 83

E

Eastman Kodak 34
Egghead 22
Electronic Data Systems 13
Elf Aquitaine 83
Enichem 83
Evotec 70

F

Federal Express 34
Fiat 82
Fidelity Emerging Markets Fund 102
Fluid Thinking 86
Food Lion 89
Ford 47, 82
Foreign & Colonial Investment Trust 54
Foxboro 90
Franklin Templeton Fund 102
Fuji Heavy Industries 18

G

Gateway 2000 76
GE 34, 79, 94
GM 45, 47, 82
Geodyssey 69
Glaxo 70
Global Power Investments Fund 90
Goldman Sachs 44, 54, 92, 94
Grand Metropolitan 50
Grant & Thornton 105
Green Bay Packers 6
Grupo Carso 102
Grupo Tribasa 102

H

Harley-Davidson 39
Harris Associates 46
Hertz 104
Hewlett-Packard 13
Hill Refrigeration 92
Hilton Hotels 104
Hitachi 72
Hoechst 70
Home Depot 88
Honda 18, 47
Honeywell 50
Hunter Marine 87
Huntsman Specialty Chemicals 83
Hussmann 92

I

IBM 13, 18, 34, 72, 76, 87
ICA 58
ICI 83
Illinova 93
Infobahn Xpress 13
Intel 8, 13, 69, 76
Intergraph 13
International Data 22
International Rectifier 96
ITT 92

J

James Capel 102
J.C. Penney 48
Jensen Securities 90
Jerrell 48
John Beall 90
Johnson & Johnson 50

K

Kemper 94
KKR 50
KPMG Peat Marwick 105

L

Lehman Brothers 96
Lexington Emerging Markets Fund 102
Littion Industries 50
Loews 54
Lotus Development 22, 50, 72
Lucky Stores 89

M

Margaux 92
Mars 46
Matsushita 44
McGraw-Hill 105, 109
MCI Communications 104
MediGene 70
Mellon Bank 50
Mercedes-Benz 58
Merck 96
Mercury Communications 6
Merrill Lynch 30, 54
Meta Group 72
Micro Warehouse 76
Microsoft 8, 13, 44, 69, 72, 86
MMS International 109
Mobil Oil 83
Montgomery Emerging Markets Fund 102
Morgan Stanley 62, 93
Morningstar 102
Morphosis 70
Motorola 69, 72, 76, 96, 112
M.R. Weiser 105

N

National Football League 6, 79
NatWest 54
NBC 79
Neiman Marcus 8
Network Connection 69
New Line Cinema 79
Niagara Mohawk Power 93
Nike 18
Nissan 82
North Sails 86
Northwest Airlines 104
Novell 22

O

Ockam Instruments 86
Ogilvy & Mather 46
Ortho Pharmaceutical 50
Otis 92

P

Pacific Gas & Electric 93
PacifiCorp 93
PaineWebber 76, 92
Panasonic 58
PC Complete 76
Pemex 58
PepsiCo 34
Pet 50
Peugeot 82
PGA 45
Philips Electronics 44
Phoenix Information Systems 90
Pillsbury 50
Playboy Enterprises 104
Prudential Insurance 101

Prudential Reinsurance 50
Public Service Co. of Colorado 93

Q

Quantum Fund 90
Quantum India Fund 90
Quantum Industrial Holdings 90

R

RauCon 70
Regeneron 50
Renaissance Cars 47
Renault 82
Robertson Stephens Emerging Markets Fund 102
Robinson Humphrey 76

S

Saatchi & Saatchi 18, 4
Salomon Brothers 72
Saperstein, Goldstein, Demchak & Bailor 88
SAS Institute 13
S.B.S. Financial Group Schering 70
Science Applications International 86
Scudder New Asia Fund 102
Scudder, Stevens & Clark 102
S.G. Warburg 62, 83
Sharp 22
Shoney's 88, 89
Sila 82
Silicon Graphics 13
SNC Capital Management 94
Sony 79
Soros Fund Management 90
SoundView Financial Group 72
Sprenger & Lang 88
Sprint 6
Standard & Poor's 105
State Farm 88
Subaru 18
Sugen 70
SunAmerica 94
Susan Powter Corp. 48

T

Tandy 34
Tektronix 90
Tele-Communications 7
Time Warner 69, 79
Toshiba 72, 76
Toyota 18, 82
T. Rowe Price 93, 94
TRW 13
Turner Broadcasting System 79

U

UB 90
Union Carbide 83
United Airlines 104
United Artists 89
USAir 89, 104
U S West 44

V

Volkswagen 58, 82

W

Wal-Mart 50
Walt Disney 47
Western Digital 34, 76
Westinghouse Electric 6

X

Xerox 22, 34

Z

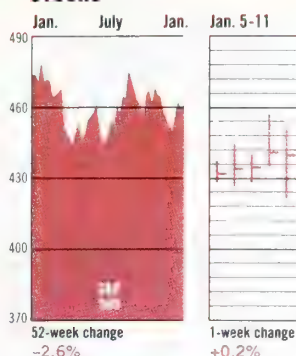
Zacks Investment Research 92

Investment Figures of the Week

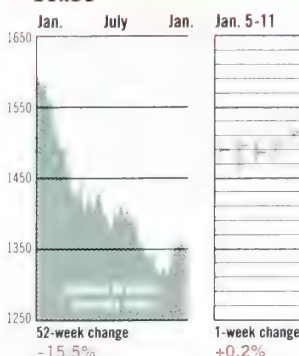
MARKET COMMENTARY

Economic woes continued in financial markets. Traders remained unconvinced that the government's plan would head off a recession and stabilize its markets. The New York Fed jumped in to support the peso on Jan. 9 and President Clinton pledged support on Jan. 11, the peso steadied and the stock market halted their plunge. U.S. record earnings from Mexico sparked a rally on Jan. 11, but stocks ended Jan. 11 down 1.1%. The long bond rallied on reports of a rate cut.

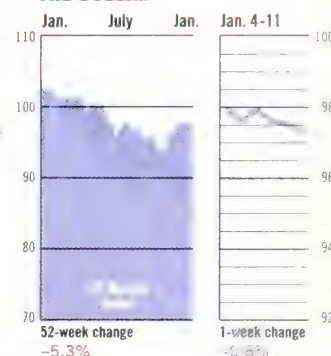
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

INDEX	Latest	% change	
		Week	52-week
DOW JONES INDUSTRIALS	3862.0	0.1	0.3
SMALL-CAP COMPANIES (S&P MidCap Index)	169.9	0.5	-5.2
MID-CAP COMPANIES (Russell 2000)	248.2	0.2	-4.6
LARGE-CAP COMPANIES (Russell 3000)	264.5	0.3	-3.3

INTERNATIONAL STOCKS	Latest	% change (local currency)	
		Week	52-week
DOW JONES (FINANCIAL TIMES 100)	3049.4	-0.1	-9.6
NIKKEI INDEX	19,548.5	-0.7	4.0
DAX (TSE COMPOSITE)	4186.7	0.8	-6.0

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.75%	5.84%	3.02%
30-YEAR TREASURY BOND YIELD	7.84%	7.85%	6.18%
S&P 500 DIVIDEND YIELD	2.80%	2.81%	2.61%
S&P 500 PRICE/EARNINGS RATIO	17.0	17.0	23.2

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	457.5	457.6	Positive
Stocks above 200-day moving average	34.0%	32.0%	Positive
Speculative sentiment: Put/call ratio	0.57	0.60	Neutral
Insider sentiment: Vickers sell/buy ratio	1.06	1.06	Positive

BLOOMBERG FINANCIAL MARKETS

INDUSTRY GROUPS

WEEK LEADERS	% change		Strongest stock in group	% change		Price
	4-week	52-week		4-week	52-week	
AIRCRAFT & SPACE	12.7	-15.0	NAVISTAR INTERNATIONAL	19.6	-33.0	16 ³ / ₄
SHIPBUILDING	12.1	4.6	STONE ISLAND	21.3	55.8	18 ¹ / ₂
TELECOMMUNICATIONS	12.1	-41.6	CENTEX	13.2	-43.4	23 ⁵ / ₈
PHARMACEUTICALS	12.1	3.1	COLUMBIA/HCA HEALTHCARE	12.4	7.7	38 ⁵ / ₈
COMPUTER SOFTWARE	10.8	-13.8	MORTON INTERNATIONAL	13.9	-7.9	29 ⁵ / ₈

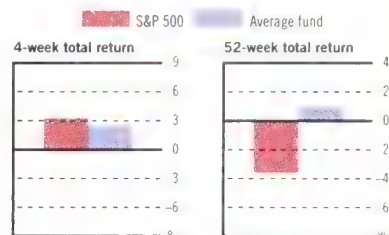
WEEK LAGGARDS	% change		Weakest stock in group	% change		Price
	4-week	52-week		4-week	52-week	
TELECOMMUNICATIONS	-3.6	-19.3	THE LIMITED	-6.5	-2.1	17 ⁷ / ₈
MINING	-3.1	-27.2	SANTA FE PACIFIC GOLD	-13.3	NA	11 ³ / ₈
RETAIL	-2.3	-5.7	LIZ CLAIRBORNE	-19.3	-23.3	17 ¹ / ₄
ENERGY	-2.2	-24.0	HELMERICH & PAYNE	-2.4	-13.1	25 ³ / ₄
TELECOMMUNICATIONS	-1.9	-15.3	SPRINT	-9.4	-19.3	26 ⁵ / ₈

MORNINGSTAR INC.

MUTUAL FUNDS

TOP PERFORMERS	Week total return	%	LAGGARDS	Four-week total return	%
AMERICAN FUND	11.7		WRIGHT EQUIFUND-MEXICO NATL. FID. EQTY.	-41.2	
AMERICAN SPECIAL EQUITIES	10.9		FIDELITY LATIN AMERICA	-27.6	
AMERICAN HARTWELL EMERG. GR. A	10.2		TCW/DW LATIN AMERICAN GROWTH	-26.9	
AMERICAN REALTY					

TOP PERFORMERS	Week total return	%	LAGGARDS	52-week total return	%
AMERICAN COMMUNICATIONS & INFORM. A	28.1		MONITREND GOLD	-55.5	
AMERICAN SMALLER COMPANIES	23.0		STEADMAN OCEANOGRAPHIC TECHNOLOGY	-39.4	
AMERICAN TECHNOLOGY A	22.8		STEADMAN AMERICAN INDUSTRY	-39.0	



RELATIVE PORTFOLIOS

Amounts represent the value of \$10,000 and one year ago portfolio

Figures indicate percentage total returns

Foreign stocks
\$10,863
-1.37%

Money market fund
\$10,485
+0.30%

U.S. stocks
\$9,990
+0.56%

Gold
\$9,590
-1.79%

Treasury bonds
\$8,704
+0.77%

Figures on this page are as of market close Wednesday, Jan. 11, 1995, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of market close Jan. 10.

Mutual fund returns are as of Jan. 6. Relative portfolios are valued as of Jan. 10. A more detailed explanation of this page is available on request. r=revised NA=Not available

A CORPORATE DIET FOR UNCLE SAM

Bureaucratic, hierarchical, wasteful, inflexible, and alienated from its users: No, it's not Corporate America in the 1980s. It's American government in the 1990s. A great debate is roiling Washington about the proper size and role of government in the lives of 250 million Americans. But there's no consensus—beyond the notion that Uncle Sam must slim down. Everything else is up for grabs.

Early signs are troubling. A new *BUSINESS WEEK* poll shows that the public is profoundly ambivalent about cutbacks (page 34). That could easily bring about political polarization. In Congress, there are already signs of playing slash and burn for partisan points. The game seems to be to zero out your opponent's political base while protecting your own constituencies. Prepare for the elections of 1996.

Our advice: Don't play that game. Successful reinvention of government—based on efficiency, not politics—would unleash massive resources for savings, capital accumulation, and income growth. A serious effort to make government more efficient would bring a quantum leap to America's position in the world economy.

Before politicians start hacking away at the federal bureaucracy, they should put in a call to Ford, Motorola, and Compaq. These are just a few of the hundreds of companies that restructured in the '80s to become efficient competitors. Newt Gingrich and Al Gore are both lucky to have a wealth of how-to information already at hand from the private sector. They should use it.

The secrets of corporate downsizing are well known. Before blindly cutting 10% of everything, rethink the mission of each level of government. Ask what must be done inside the government and what could be farmed out. Reengineering

is as important as trimming. Mayors know that cities must police the streets themselves but that garbage can often be more cheaply collected privately. Congress knows that the U.S. must have a strong military, but does Uncle Sam have to be in the business of grazing cows? Privatizing some public lands in the West could generate billions.

A second lesson from business concerns delivery. Companies are now outsourcing anything that is not a core competency. If the government wants to provide housing to the poor or medical care for veterans, must it retain huge bureaucracies to do the work, or could vouchers be used to provide services in the private sector? Food stamps are successful vouchers. Job training, veterans' health care, and many kinds of public education might better be delivered through them.

The private sector shows that flexibility is key to improving productivity. Cutting layers of management and giving power to lower-rung employees closest to the customer are fundamental. That means new civil-service rules. Today, there is virtually no accountability in many government offices.

Finally, the dangers of going too far in restructuring are commonplace in downsizing companies. Merely shifting functions and excessive decentralizing are classic mistakes. If Washington does is transfer welfare, health services, and regulation to the local level, it won't work. Fifty regulatory bodies are not more efficient than one.

The goal in the current debate over reforming government is cutting costs, not getting even politically. Until very recently, middle-class workers had not seen real income gains for two decades. They want to pay less for government services. Corporate America has shown how to accomplish this kind of goal. Get on with it, Washington.

WILL THE REAL ALAN GREENSPAN STAND UP?

On Tuesday, Jan. 10, Federal Reserve Chairman Alan Greenspan testified to Congress that the actual inflation rate could be as much as 1.5 percentage points below the official figure. *BUSINESS WEEK* made the same point in "The real truth about the economy" (Cover Story, Nov. 7, 1994). The policy implications of Greenspan's direct attack on price statistics cannot be underestimated. Everyone should face the implications, including Greenspan himself.

For starters, Greenspan suggested that policymakers should use the lower figures in Social Security and cost-of-living calculations. That would decrease the federal budget deficit by up to \$150 billion over the next five years. That's real savings.

But Greenspan's admission that he believes inflation to be much lower than the current figure raises a question: Why does the Federal Reserve keep raising interest rates? Just one day after Greenspan testified to Congress that the consumer price index overstated inflation, new numbers showed

that core inflation in 1994 was only 2.6%, the lowest since 1965. This means the true rate of inflation is at most 2%, and perhaps as little as 1%.

Bond vigilantes can argue that's all history. With capacity and labor tight, inflation is bound to rise in the future. Maybe so. But an inflation rate of 1% to 2% means that real interest rates are already sky-high. The real three-month interest rate is between 3.5% and 4.5%, a level that has historically been a sign of impending recession. With credit so costly, the economy is nearly guaranteed to slow in the months to come without any additional hikes in rates. By repeatedly warning that inflation was about to erupt, the Fed has had the perverse effect of raising inflationary expectations. It's time for Greenspan to tell the financial markets what he really believes: that inflation is extraordinarily low. That's the best way to lower inflationary expectations and preserve economic growth into 1996.

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PAGE 62

An Inside Look at George Fisher's Strategy



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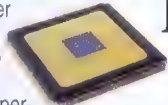
Steve Archuleta
Director, Systems for Mass
Markets Service Delivery
U.S. WEST, Phoenix

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like me. I take my risks on the weekend."

Power Macintosh. The business Macintosh.



COVER STORY

Key to Kodak's growth strategy is getting its world-class imaging technology into consumer products

page 62

BusinessWeek

JANUARY 30, 1995

Cover Story

62 KODAK'S NEW FOCUS

After barely a year at the helm, George Fisher has shaken up Kodak as never before, selling off health units, refocusing on imaging, and slashing debt. He has also given staffers hope that Kodak has a future beyond repeated restructurings. But laying the foundation for a turnaround is one thing. Actually delivering it is another

68 DUPE-IT-YOURSELF

Kodak's CopyPrint instant enlargement system is a smash

News: Analysis & Commentary

30 BLOWUP AT BRIDGESTONE

The tire company thought it could contain a labor dispute. Instead, the conflict became an international incident

32 THE STATE OF BILL CLINTON SPEECH

Can he find a new voice? Comeback hopes may hinge on his message

33 A NEW GENE McCARTHY?

Democrat Robert Casey is pro-life, pro-religion, and anti-Clinton

34 TAX CUTS: TOO MANY SCALPELS

Reduction fever is gripping the Hill, but the final plan may be modest indeed

35 A PENSION FUND GETS GUTSY

CalPERS sees huge returns from increasing its stock holdings

36 COMMENTARY

A hike in the minimum wage wouldn't do much to help the poor

38 INTEL BARELY BREAKS STRIDE

Despite the hit from the Pentium bug, revenues are up dramatically

39 NET-SURFING NUNS

They're part of PC makers' pitch to the MTV generation

40 JAPAN: HOPE BENEATH THE RUBBLE

Ironically, the quake could give the economy a long-term boost

42 IN BUSINESS THIS WEEK

Kmart's Antonini, natural-gas prices, Orange County, Saatchi, Tyson retires, First Fidelity, Nintendo vs. Samsung

International Business

46 EUROPE

The finance vigilantes are closing in on Europe's weaklings

47 MEXICO

Washington to the rescue. But now about the price...

48 INDIA

After four rocky years, free-market reforms are stirring up the nation's long-stagnant economy

50 INTERNATIONAL OUTLOOK

It's tooth and claw in Moscow, where the reformers are biting back

Economic Analysis

22 ECONOMIC VIEWPOINT

Roberts: Why should the GOP waste time tinkering with the income tax? Better to abolish it altogether

26 ECONOMIC TRENDS

Inside buyers are acting bullish, imports and inflation, booze and hard times, Beijing blinks on trade

27 BUSINESS OUTLOOK

Don't be fooled. The economy is still too hot for the Fed

86 FAT PROFITS, SKIMPY PAYCHECKS

Workers aren't feeling the boom, but closer look at the numbers suggests they will—eventually



WHY'S NEW ECONOMY
Inflation is bringing
and investment page 48



PLAIN PIZZA
Domino's Tom
Monaghan nearly
let his fondness for
extravagance
destroy the chain.
But he's a changed
man now page 37



L.T. GOES VR
The ex-grid
star says his
virtual-reality
venture is
ready to romp
page 84



'SILICON ALLEY'
Manhattan, the home of
many media giants, is now
turning into a haven for
multimedia startups
page 82

THE BIG INCOME SHIFT
Why workers are making
less while companies are
making more page 86

Government

WASHINGTON OUTLOOK

ton could end up looking like the
y on immigration

People

DOMINO'S TOM MONAGHAN

is simplifying both his company
his lifestyle, and the changes are
ting to pay off

Corporation

LABOW'S STEELY RESOLVE

dyne has put a poison pill in place,
that won't stop WHX's chief from
suing the pension-rich conglomerate

Science & Technology

THE FDA HOOKED ON CAUTION?

aces fresh wrath from the right
r charges of excessive regulation
slow approval of new products

DEVELOPMENTS TO WATCH

y-power pagers, butterflies and
s, authenticating toons with DNA,
monal pick-me-ups for seniors

Finance

76 DERIVATIVES' DIMMED GLAMOUR

Still growing despite the bond rout of
last year, the market is leaning to less
exotic, less lucrative products

78 HOME RISKY HOME

The Federal Home Loan Bank system's
"innovative" investments give pause

79 PILGRIM'S PROGRESS?

The Pilgrim mutual funds are deathly
ill, but Robert Stallings sees a cure

80 INSIDE WALL STREET

Cadbury is sweet-talking Dr Pepper
Zooming in on interactive TV
Nucor, the No. 1 steal in steel

95 INVESTMENT FIGURES OF THE WEEK

Information Processing

20 TECHNOLOGY & YOU

The trouble with Microsoft's Bob

81 IBM'S PARALLEL POWERHOUSE

The new SP2 may wean Big Blue off
its mainframe dependency

82 NEW YORK: MULTIMEDIA MECCA

Its startup scene rivals those of
Seattle and Hollywood

Sports Business

84 CAN L.T. SACK THE SKEPTICS?

The former Giants linebacker raised
millions with an IPO last year. Now
he has a product

Personal Business

90 PHONING: Long-distance deals

SMART MONEY: Low-fee money funds

AUTOS: Three for the road—or trail

Features

6 UP FRONT

10 READERS REPORT

12 CORRECTIONS AND CLARIFICATIONS

16 BOOKS

Champy: *Reengineering Management*;
The Mandate for New Leadership
Mariani with von Bidder: *The Four
Seasons: A History of America's
Premier Restaurant*
Marcial: *Secrets of the Street*

93 BUSINESS WEEK INDEX

94 INDEX TO COMPANIES

96 EDITORIALS

Simplifying taxes would save a bundle
Don't hike the minimum wage

Up Front

EDITED BY LARRY LIGHT WITH RUTH COXETER

BILL'S BUNCH

WHY RON BROWN WANTS TO STAY PUT

GOP SNIPING AGAINST RON Brown may have the unintended effect of keeping him in his beloved job as Commerce Secretary a while longer. Bill Clinton wants to shift Brown over to head his reelection committee—an uphill task that Brown doesn't relish. Political savants say the latest flap over Brown's finances makes it more likely Clinton will keep Brown at Commerce, where he's the toast of Corporate America, rather than move him closer to the President.

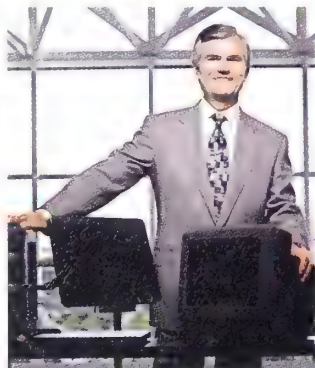
House Government Reform & Oversight Committee Chairman William Clinger Jr.



BROWN: More flak bursts

(R-Pa.) wants Brown to appear before his panel. Otherwise, Clinger may push for the Justice Dept. to appoint an independent counsel. According to *The Washington Post*, an ex-business partner of Brown paid \$190,000 of his personal debts, which his lawyer calls payment for Brown's share of the business.

Brown, who dubs the latest imbroglio "much ado about nothing," says he is "more helpful to the President and the economy where I am." To reinforce that, Brown is stepping up his trade-mission itinerary: He left on Jan. 14 for India with 25 U.S. CEOs. Future jaunts: the Middle East, China, South America, and Africa. *Douglas Harbricht*



PFEIFFER: Gambled big, won

SUPPLY & DEMAND

YES, COMPAQ, THERE IS A SANTA CLAUS

COMPAQ COMPUTER'S RISKY inventory gamble seems to have paid off. It made a massive bet on the holiday buying season—doubling the year-before inventory to \$2.3 billion. With Compaq set to report fourth-quarter earnings on Jan. 25, word is that the company really moved the goods. Dean Witter Reynolds analyst Eugene Glazer expects earnings to be up 65%.

Demand for PCs helped a lot, and Compaq had product waiting on the shelves. Also buoying Compaq: the 1994 caution of IBM, which got

TALK SHOW "The current media definition sometimes seems to be: A derivative transaction is any financial transaction in which a large amount of money is lost."

—Mary Shapiro, Commodity Futures Trading Commission chief

STREET NEWS

HEY, LET'S ALL SUE PRU!

PRUDENTIAL SECURITIES IS even under attack from brokers. In a just-filed class action, a former Pru broker says the firm's misleading sales claims for its disastrous limited partnerships have hurt his ability to make a living in the securities business.

It's rare to find brokers suing a firm for allegedly lying to them that an investment product they sell is not risky. William

Mandel of Boca Raton, Fla., says he got his clients to buy nearly \$2 million worth of the limited partnerships. Since the partnerships' collapse in the early 1990s, he has lost at least \$400,000 in income from an "impaired reputation and lost business relationships,"

the lawsuit claims. Today Mandel, 43, works as a Dean Witter broker. His lawyer Thomas Hoadley, says some 75 ex-Prudential brokers are interested in either joining the class action or filing parallel suits.

That's bad news for Pru, which has already put \$60 million aside to pay off investors who lost money in the

Prudential Securities

partnerships as part of broad securities fraud settlement. The firm pitched 700 land and energy ventures, totaling nearly \$8 billion. A company spokesman characterizes the broker's legal action as "frivolous suit that is without merit." *Michael Schroeder*

burned in 1993 after making its own big inventory wager. Last year, Big Blue grossly underestimated demand for its Aptiva PC. During 1994's first nine months, Compaq seized IBM's PC market-share lead. International Data analyst Eric Lewis figures Compaq ended the year with a 10.2% share, IBM with 8.7%. Few now laugh at Compaq CEO

Eckhard Pfeiffer's goal: to double his nearest competitor's share. A Compaq executive says rivals now had better follow its fat-inventory policies.

One snag: Compaq risks mutiny by margin-squeezed distributors. And by retailers—some were miffed by pre-Thanksgiving shipment delays due to shortages of monitors. *Peter Burrows*

THE LIST CAR THEFTS

Buy a cheap car and worry no more about it being broken into or stolen, right? Not quite. The worst record among newer cars belongs to the VW Cabriolet, a small, soft-top runabout. It's easier to slit open a con-

vertible's roof. The Cadillac, of course, has snob appeal. Ditto the sporty Mustang.

But the unexciting Honda Civic?

Go figure. The least-hit list is more understandable: Those cars are family-oriented, and crooks don't find them sexy.



VW CABRIOLET Here today...

MOST FREQUENT TARGETS*

1. VOLKSWAGEN CABRIOLET	4.6
2. FORD MUSTANG CONVERTIBLE	3.9
3. CADILLAC DE VILLE TWO-DOOR	3.4
4. FORD MUSTANG	3.3
5. HONDA CIVIC TWO-DOOR	2.5

LEAST FREQUENT TARGETS*

1. CHEVROLET CAVALIER STATION WAGON	0.29
2. FORD TAURUS STATION WAGON	0.32
3. PONTIAC GRAND PRIX FOUR-DOOR	0.32
4. OLDSMOBILE CUTLASS FOUR-DOOR	0.34
5. OLDSMOBILE CUTLASS TWO-DOOR	0.34

*No. 1 through 5, which insurance claims exceed average for all U.S. '91-'93 autos insured

DATA: HIGHWAY LOSS DATA INSTITUTE

A photograph of a simple wooden table. The table has a dark, possibly stained or painted, top surface. The legs are made of a lighter-colored wood. The table is positioned in the foreground, and its reflection is visible on the floor below it. The background is a plain, light-colored wall.



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Up Front

SLUGFESTS

CAUTION: DUELING SWEAT MACHINES

THE BOOMING HOME-FITNESS industry is developing both well-defined abs and sharp elbows. Rivals are churning out infomercials that snipe at each other's exercise contraptions. But nothing tops the rancor between the makers of two hot-selling—and similar—new machines where you push on both pedals and handlebars for a total body workout.



The maker of HealthRider, ExerHealth in Salt Lake City, accuses Icon, the manufacturer of CardioGlide, of unethically slamming HealthRider in a fitness magazine that has links to Icon. *Shape* magazine's December issue

ICON AD: Barbs and belles

knocked HealthRider as being possibly harmful to the lower back—and didn't mention its relationship with CardioGlide. Until November, when Boston's Bain Capital purchased it, Icon, based in Logan, Utah, was owned by Weider Health & Fitness, *Shape*'s publisher. Two Weider execs, though, now sit on Icon's board. "They didn't disclose this," gripes Gary Smith, chief executive of ExerHealth.

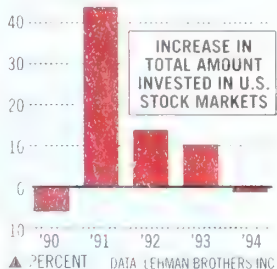
Icon denies having anything to do with the article. And *Shape* Editor-in-Chief Barbara Harris says an independent expert rated HealthRider. Plus, Harris notes, the magazine also gave a thumbs-down to another Icon product, Jane Fonda's Walk to the Music treadmill.

This flareup is in the nasty spirit of the half-hour infomercials that sell a lot of this stuff. CardioGlide ads say HealthRider is too expensive; HealthRider's say CardioGlide isn't as effective. And with family-oriented baby boomers increasingly spending more time at home and less in the gym, conflict in this \$2.5 billion market is sure to intensify. □

THE BIG PICTURE



A lackluster stock market over the past year has slowed the huge inflow of investment. The postrecession surge of money into the market ebbed as rising interest rates made other investments more attractive.

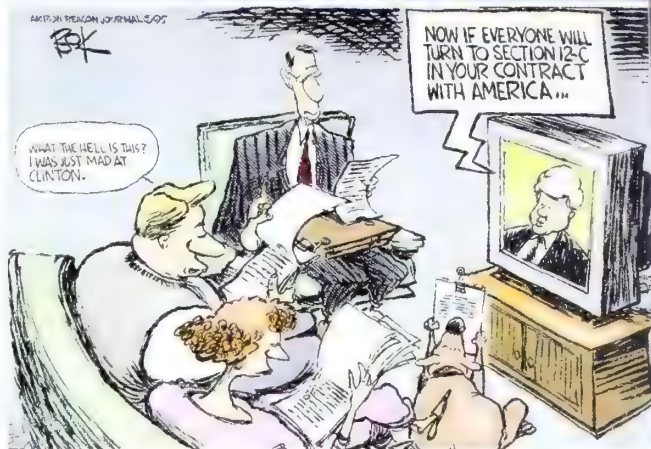


WARM PLASTIC

HEARTLESS BANKERS? MAYBE NOT

THE AGE OF NEWT IS A friendless time for a variety of causes. But they now have a pal in MBNA America. The bank offers what it calls "a revolutionary new credit card" that gives a dime for each charge to 32 organizations. Recipients range from such liberal favorites as the Children's Defense Fund, made famous by Hillary Rodham Clinton, and the Rainforest Action Network to the more mainstream Ronald Mc-

DRAWN & QUARTERED



ENDANGERED SPECIES

A VERY TONY SMOKE-FILLED ROOM

TALK ABOUT OUTCASTS. IN AN increasingly tobacco-antagonistic society, cigarette puff-ers pale next to cigar smokers. But now, there's a sanctuary for the stogie crowd, albeit a pricey one.

Havana, a private Beverly Hills club for cigar smoking, opens in March. With a charter membership that spans the generations from comedian Milton Berle to actor Jason Priestley of *Beverly Hills 90210* and is open to both sexes, the club costs \$2,000 to join and \$150 per month. Members have their own private humidors on premises, where they also can eat and drink. "This is an incredible oasis," says Joe Pantoliano, an actor (*Risky Business*,

The Fugitive) who co-owns the joint with veteran restaurateur Stanley Shuster.

To them, the club concept is the best defense against the march of antismoking legislation. A number of restaurants around the country host cigar nights, yet new local



CUBA 90210: Cigar smokers Shuster, Berle, Pantoliano

laws ban any smoking in public places. Arnold Schwarzenegger closes his entire restaurant one night a month to avert Santa Monica's new ordinance and host his stogie shindig. *Jennifer Holland*



FOCUS: MBNA's cause card

Donald Children's Charities. Ads for the GlobalFocus Visa card evoke the counterculture heyday by saying it's in the tradition of struggles

for civil rights and nuclear disarmament. Yet Newark (Del.)-based MBNA contends its pitch isn't ideological; it just wants to help those who do good and thinks this is a profitable niche. In fact, it also issues an affinity card for the American Legion. Regardless, MBNA seems to have learned to woo the left from a former affinity client, Working Assets Funding Service. Its beneficiaries include a few groups MBNA gives to, but adds some more controversial ones dedicated to gun control, gay rights, and abortion rights. *Joseph Weber*



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A NOTE ON SCREEN NAMES

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term event. As "A better way to pay for college" (Editorials, Jan. 9) notes, until recently, runaway tuition hikes were business as usual in higher education. Historically, many colleges implemented program initiatives outside of formal strategic planning, with little thought given to setting priorities, controlling waste, and imposing significant fiscal restraint.

At Babson College, we created an Office of Quality and use quality-management principles to strive for the lightest standards while curtailing waste.

In December, 1992, I made a public commitment to limit Babson tuition increases to no more than 1% to 1.5% above the consumer price index. The time has come for colleges and universities to be aggressive in keeping their financial houses in order while providing real value in higher education.

William F. Glavin
President
Babson College
Babson Park, Mass.

DO IRAS TAKE CASH OUT OF UNCLE SAM'S POCKET?

Regarding to your article "IRAS: No spur to net savings" (Economic Trends, Jan. 9), it gets tiresome to read such statements as: "IRAS clearly cost the U.S. Treasury money." IRAS don't cost the Treasury money, they merely delay the collection.

On the subject of people simply shifting savings, this is no doubt true. But the character of the shift is probably short-term money in savings to long-term types of investments. And even if it isn't, what's wrong with building up the Treasury Dept.'s nest egg?

Frank P. Ferrentino
Bloomfield, N.J.

FANS AND FOES OF A FLAT TAX

Christopher Farrell's commentary, "A jumble only a flat tax can untangle" (News: Analysis & Commentary, Jan. 9), was nice. But why settle for a flat tax when we have a chance to see

real tax reform—a national sales tax.

The national sales tax virtually eliminates the IRS, tax accountants, tax lawyers, H&R Block, and much of our bloated government.

David Beeme
Virginia Beach, Va

Along with an obscenely bloated government, a flat tax would greatly shrink our massive underground economy. However, wonderfully logical it would be if our politicians could only get their hands on more of our money if we made more of it ourselves.

Alas, the true fatal flaw of the flat-tax proposal is the very logic that makes it a brilliant—if long overdue—concept. The entrenched power base of tax attorneys and government dependents will never go for it.

Dave Terrill
Gold River, Calif.
DaveT24985@aol.com

A flat tax is a blatant attempt to lower taxes for the rich.

Harold R. Slossor
Schererville, Ind

WHAT NEWT'S CONTRACT REALLY SAYS

I'm surprised and appalled by your article "We polished the crystal ball, and...Contract with America" (Up Front, Jan. 9). It seems to me inexcusable that you do not make the distinction that Newt Gingrich's promise is to bring the issues in the Contract with America to a vote, not a promise to pass the issues.

Gary L. Johnson
Minneapolis

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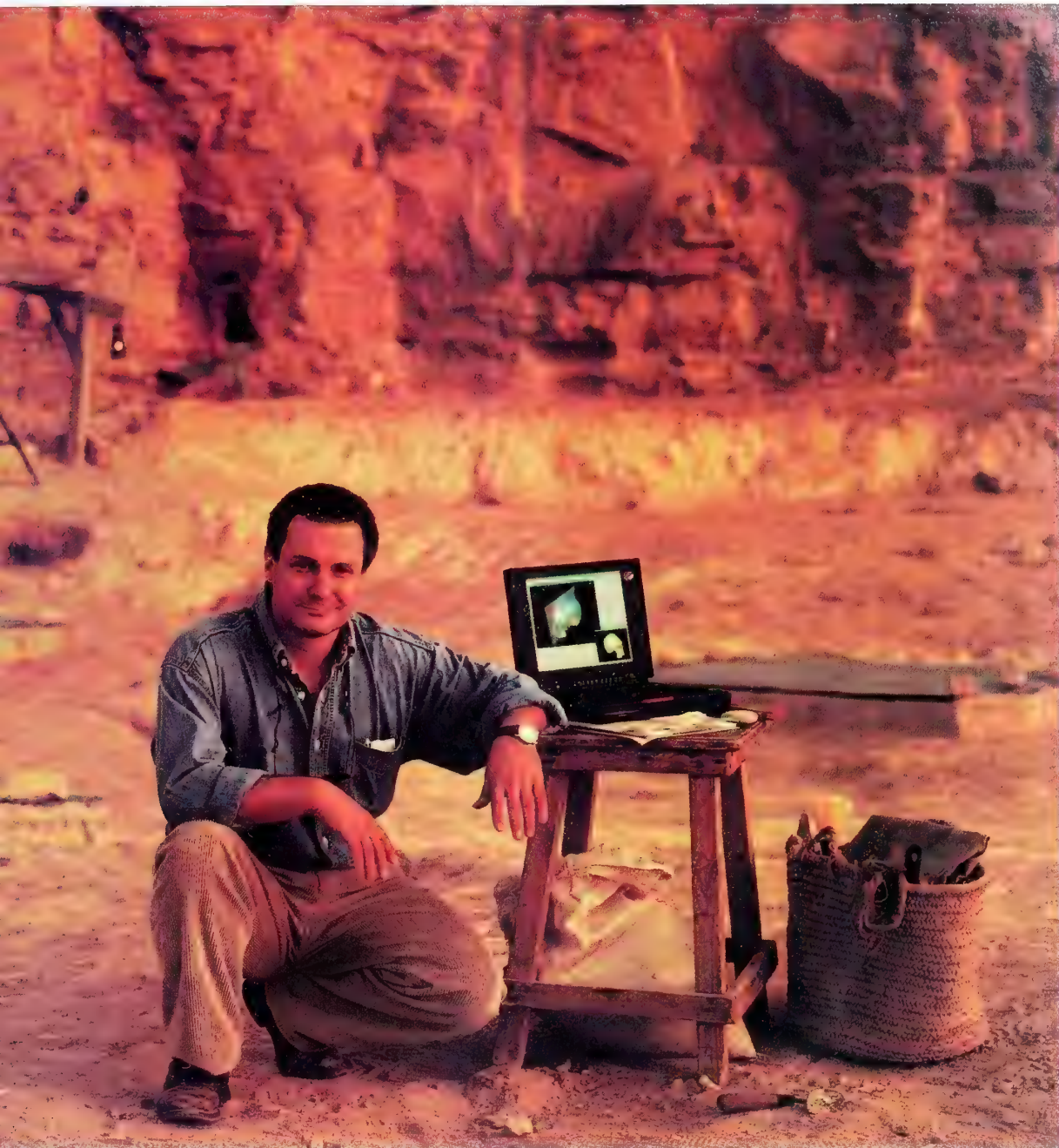
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Thomas Quarry
Casablanca, Morocco



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REENGINEERING MANAGEMENT

The Mandate for New Leadership

By James Champy

HarperBusiness • 212pp • \$25

REENGINEERING: WHAT HAPPENED?

Two years ago, a book was published that helped define one of the most influential management concepts to emerge in years. *Reengineering the Corporation*, by James Champy and Michael Hammer, sold nearly 2 million copies in 14 languages, making it the best-selling business book since *In Search of Excellence*.

Reengineering inspired executives and managers in thousands of companies to start rethinking and redesigning such basic business practices as customer service, order fulfillment, and product development. And for some, reengineering brought quantum improvements in productivity, customer satisfaction, and quality while significantly cutting costs. Champy, chairman of CSC Index Consulting Group in Cambridge, Mass., and Hammer have become world-renowned management gurus.

What can an author possibly do for an encore? Champy, flying solo here—Hammer will bring out two reengineering books later this year—opens with a startling admission: “Reengineering is in trouble.” Despite notable successes at such companies as Bell Atlantic Corp. and Federal Express Corp., many reengineering efforts have fallen far short, Champy concedes. He cites one study in which companies failed to attain goals of cost reduction and market-share growth by as much as 30%. “The revolution we started has gone, at best, only halfway,” he writes. “I have also learned that half a revolution is not better than none. It may, in fact, be worse.” While countless managers have been persuaded to reengineer, too many have had poor or disastrous results.

So Champy examines the reasons reengineering fails—and concludes that the key problem is management itself. Operational work can’t be reengineered without changing the way managers do their jobs. Consequently, this book is less about reengineering than about leadership, teamwork, empowerment, and corporate culture.

What does Champy have to add on such overworked topics? Mainly some valuable context. Radical change is impossible unless managers know how to, in his words, “organize, inspire, deploy, enable, measure, and reward the value-adding operational work.” The lack of these skills has been a stumbling block to nearly every reengineering initiative.

Through extensive interviews with managers who have lived through generally successful efforts at such companies as Wisconsin Energy, Intel, and Frito-Lay, Champy tries to show readers how to clear the hurdles. Survivors of other reengineering efforts are bound to empathize with one manager who tells Champy: “We don’t really know how to do reengineering in our company; so what we do is, we regularly downsize the company and leave it to the three people who are left to figure out how to do their work differently.”

Like so many sequels, however, *Reengineering Management* lacks the path-breaking content and passion of the original. Worse, readers have to slog through long transcribed passages of interviews that are often redundant or unrevealing. The oral-history approach just doesn’t work here—and roughly 75 pages are given over to the device.

That’s not to say that Champy didn’t discover some exceptionally articulate managers with worthwhile things to say. Among them are Hewlett-Packard’s Jim Olson, Intel’s Kirby Dyess, and 3M’s Leon Royer. They make you realize that reengineering can transcend what it too often becomes—a heartless exercise in downsizing.

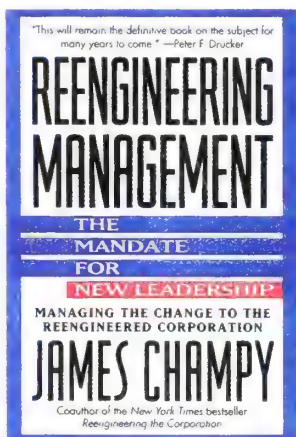
Dyess, Intel’s vice-president for human resources, speaks eloquently of the need to redeploy valuable people whose jobs are wiped out by reengineering. Royer, 3M’s executive director of organizational learning services, uses the metaphor of a hockey team to describe how new leaders must view their jobs. In a reengineered workplace, he says, leadership “switches back and forth depending on who has the puck. And where is the ostensible leader, the coach? Sitting on the sideline without skates. A coach can’t tell his skaters where to take that puck. He can train them, psych them, prepare them. But when the buzzer sounds, it is the team that’s out there on the ice....”

Such comments help Champy provide insights into five vital “core processes of management.” They are: “mobilizing” the troops behind an initiative, “enabling” the workforce to accomplish the change, “defining” the objectives, “measuring” performance, and “communicating” to employees throughout.

In almost all of these areas, Champy urges some critical, if not entirely fresh, rethinking. He suggests, for example, that peer review of an employee’s performance is more valuable than the old-fashioned review by the boss. Similarly, he describes companies that communicate better with workers by sharing the results of customer-satisfaction surveys once seen only by management.

Champy alternates four chapters that make the case for changes in managing with four chapters of comments from his managers. But this reveals an exasperating flaw. Although he has already defined his core processes, no one speaks to the first and perhaps most agonizing and divisive process—mobilizing employees to accept the changes reengineering entails.

Despite this missing piece, *Reengineering Management* stands as a helpful, if somewhat disappointing, companion to the first book. Managers awash in the ugly chaos of tearing apart their



**“THE REVOLUTION WE STARTED,” CHAMPY
WRITES, “HAS GONE, AT BEST, ONLY HALFWAY”**



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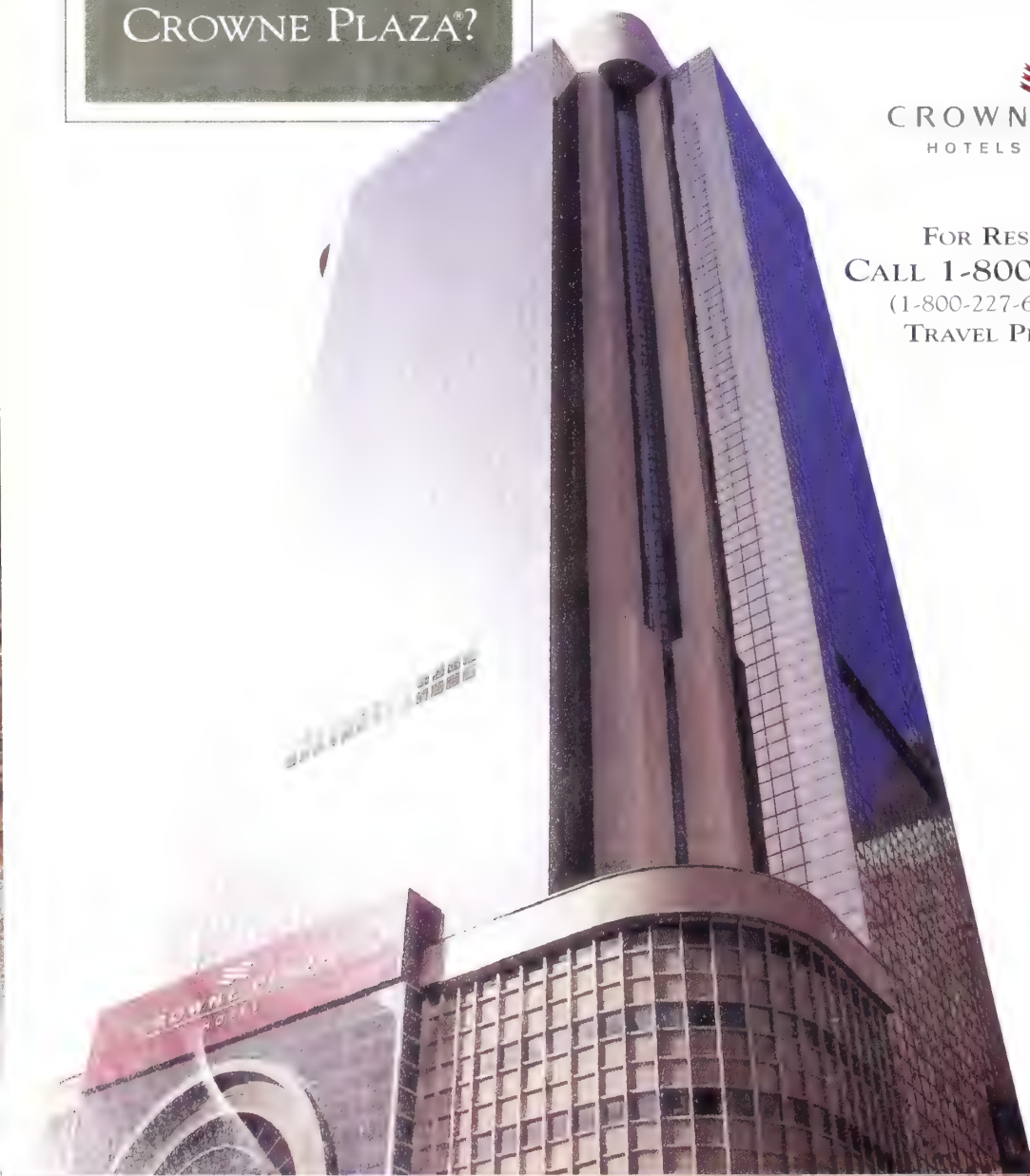
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Books

companies will find guidance and consolation here. But Champy's encore could have used a bit of reengineering itself.

BY JOHN A. BYRNE

Senior Writer Byrne covers management for *BUSINESS WEEK*.

BOOK BRIEF

THE FOUR SEASONS

A History of America's Premier Restaurant

By John Mariani with Alex von Bidder
Crown • 205pp • \$35

PATE AND POWER

Sooner or later, anybody who's anybody in New York eats at the Four Seasons, though that was hardly a foregone conclusion when it debuted in 1959. Then, only a few French and Italian restaurants served haute cuisine, and restaurant-goers ventured out to eat, not to be seen. No matter. The Four Seasons, an afterthought in the landmark Seagram Building, is now a landmark itself.

The restaurant blazed trails in design and service, fostered the power lunch, and helped foment the idea of dining as an important form of recreation and status-seeking. It also set financial records—costing \$4.5 million and charging unheard-of prices. (Nowadays, a baked potato costs \$9.75.)

Part scrapbook, part narrative, and part cookbook, *The Four Seasons* tells how it all happened. This paean is mostly fun, though it disappoints when it comes to tidbits about the alliances, snubs, and conflicts among customers. Readers must make do with, for example, a snide reference to Wisconsin conventioners who compounded the sin of arriving without jackets by wearing plaid, short-sleeved shirts. There's also the revelation that Ronald Reagan ate two desserts after a complete dinner.

You can't make a meal of the biography of a restaurant, no matter how storied. Such a book is destined to be pudding. Alas, like many a Four Seasons dessert, this one's a trifle too sweet.

BY JUDITH H. DOBRZYNSKI

BY BUSINESS WEEK WRITERS

SECRETS OF THE STREET

The Dark Side of Making Money

By Gene G. Marcial
McGraw-Hill • 238pp • \$20

VERY INSIDE WALL STREET

When insider trading last hit the headlines, it was the late 1980s, and the resulting scandals sent Mike Milken, Ivan Boesky, and other hotshot financiers to jail. Does that mean that Wall Street is now a fair game? Hardly, says Gene Marcial, *BUSINESS WEEK*'s "Inside Wall Street" columnist. In *Secrets of the Street*, Marcial makes a simple and important point: Wall Street runs on information, and if you don't have connections, you are "a turkey, an outsider trying to play an insider's game."

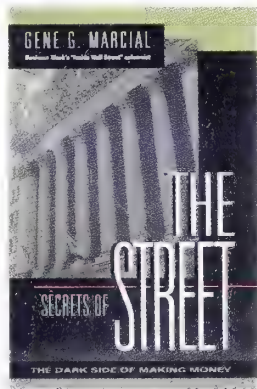
Marcial's tales of insider trading and market manipulation could confirm any paranoid's worst fears. Drawing on 20 years spent covering the Street, he recounts anecdote after anecdote showing how security analysts, brokers, and market makers

can take advantage of their inside position to make a killing for themselves or their employers. Even Wall Street's most respectable fund managers, those who run the giant institutional portfolios, are al-

ways seeking an inside edge, he asserts. Writes Marcial: "Insider trading is almost a given with money managers."

Some of the characters in Marcial's book have familiar names—Boesky, Carl Icahn, and George Soros. But in many of the juiciest stories, he uses pseudonyms to protect his sources' confidentiality. Knowledgeable

readers may make a sport of figuring out who's who. In any case, Marcial insists not only that the events took place but also that they accurately represent "what goes on on Wall Street every day of the week."



BY EDWARD C. BAIG

THE TROUBLE WITH BOB

I wanted to like Bob. As an advocate of easier-to-use PCs, I had hoped Microsoft Corp.'s new "social interface" would bring computing much closer to that lofty goal. After all, in lieu of a manual, Bob guides PC novices through a suite of software programs by replacing often cryptic icons with animated characters and cartoon images of such familiar household items as a checkbook and an address book. But while Microsoft is on to the right idea, Bob comes up a little bit short.

What's the matter with Bob? For starters, he's demanding. (I can't resist calling Bob a "he," though Microsoft uses "it.") The \$99 program—available in late March—requires 8 megabytes of RAM and 30 megabytes on your hard disk. Bob won't run on a 386 computer; and the prerelease copy we tested was sluggish even on a moderately fast 486.

TOON CASSEROLE. On the plus side, Bob boasts handsome graphics. When you first knock on the front door of Bob's house, a cartoon dog named Rover guides you to a living room. Rover tells you to launch Bob's programs by clicking on objects in the room; click on a letter box, for instance, to call up an E-mail program. You can add objects to start up other programs on your hard disk. Family members can redecorate, jump to other rooms,

or create private spaces with passwords. A warning: If you type the wrong password three times, Bob lets you create a new one—so much for real security.

Bob's main promise is that users never have to consult a manual. Instead, guides such as Rover hang out on the PC screen and steer you through Bob's applications. Over time,

GETTING TO KNOW BOB

To activate applications, you simply click on familiar objects found in different rooms.



the guides offer help only when they think you'll need it.

Some of the dozen choices for guides start off more helpful than others. The eager-to-please Java is an excitable caffeine-gulping dinosaur. The less helpful Ruby is a "mean and nasty" parrot. Scuzz is a stupid, rabid rat who obnoxiously bounces a ball in the house and has you click on such buttons as "bag it" or "cool," rather than Windows' usual "cancel" or "O.K." Those who quickly tire of these cutesy characters, as I did, can choose other guides.

Sometimes, the guides could offer a bit more help. I had to poke around to discover that I had to click on "advanced options" to adjust Bob's sound level. To create an extra-secure checkbook password, I had to click on "use a different file, change this one, or make a backup."

Still, many of Bob's programs are useful, if not particularly original. Bob reminds you of birthdays, appointments, and when bills are due. I was impressed by the letter writer, a simple word processor that makes it easy for novices to customize missives (complaints, holiday greeting, job-related). For a monthly fee, you can pay bills electronically in the checkbook.

The financial guide and household manager programs allow you to keep track of bank accounts, stocks, and maintain a record of car repairs. Bob offers advice on insurance, estate planning, even household-cleaning supplies—including a tip on removing bloodstains from carpeting. But sometimes Bob seems to confuse ignorance about computers with general dim-wittedness. A vacation packing

tip: "Wear your heaviest items rather than packing them." Under kitchen information, you are advised to "make sure that [an appliance] will fit through doors and hallways, in addition to fitting in its designated space."

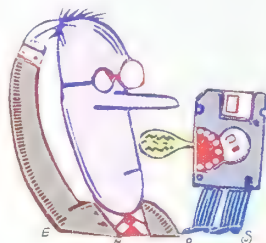
Microsoft Chairman Bill Gates acknowledges that Bob is only the beginning. Among other things, future social interfaces—perhaps for the office as well as the home—will look more realistic, remember tasks better, and employ voice recognition. But if he is to be more than a cute introduction to PC use, young Bob has some growing up to do.

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...OR WINDOWS

Jargon, from Alda Technologies (905 829-3461), is an answer to a different language problem: helping non-English speakers deal with English-language software. It lets you translate menu selections, buttons, and dialogue-box text in Windows programs into the language of your choice without changing the underlying software. The \$49 program comes with support for eight European languages built in, and users can expand their glossaries or add new languages.



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BY PAUL CRAIG ROBERTS

GOP GENERALS, TRAIN YOUR GUNS ON THE INCOME TAX



GO ALL-OUT:
Why waste
time tinkering
with today's
system, which
discriminates
against saving,
success, and
families?
Much better to
abolish it

The energy in the new House of Representatives is a marvelous thing to behold. The question is whether it will be marshaled for fundamental change or dissipated in piecemeal battles.

The great generals of history who operated on political and military fronts focused on strategic objectives and were not diverted by tactical aims. They were audacious and out-thought the enemy.

Speaker Newt Gingrich and his GOP colleagues in the House have this capability, but they must first understand that their Contract With America is nowhere near as audacious as the liberal press would have readers believe. Indeed, its achievement would represent a string of small victories without a strategic objective. Yes, it would be a good thing to cut the capital-gains-tax rate or enact a \$500 income-tax credit per child. However, these maneuvers would use up momentum while leaving the current structure of taxation intact.

A Napoleon or Wellington would realize that the same energy could be applied to revolutionizing the tax system. Why take casualties fighting over dynamic vs. static forecasts of capital-gains revenues or finding the spending cuts to offset the child tax credit when the alternative is to replace the current income-tax system—which discriminates against success, families, marriage, saving, and investment—with a flat-rate tax, a “consumed-income tax,” or a federal sales tax?

HEALTHIER EGGS. These alternatives are vastly superior to the tax goals set out in the contract. Senators Sam Nunn (D-Ga.) and Pete V. Domenici (R-N.M.) have revived the consumed-income tax that was first proposed by Treasury Secretary William E. Simon in January, 1977. Under this system, all income that is saved is exempt from taxation, thus allowing people to rapidly acquire substantial nest eggs.

Representative Richard K. Armey (R-Tex.), the Majority Leader in the House, has carefully crafted a 17% flat-rate income tax that would refurbish the economic-incentive system. It is obvious that encouraging success is superior to thwarting it and having to fill in the gap with more entitlements that cannot be financed.

Perhaps the best idea comes from Bill Archer (R-Tex.), the new chairman of the House Ways & Means Committee. Archer

wants to abolish income taxation altogether and replace it with a federal sales tax on personal-consumption expenditures. A 14% sales tax on such outlays would replace the current individual and corporate income-tax revenues. Archer's idea could be expanded to cover the payroll tax as well. Or, even better, the payroll tax could be eliminated by privatizing Social Security, thus adding to taxpayers' personal wealth.

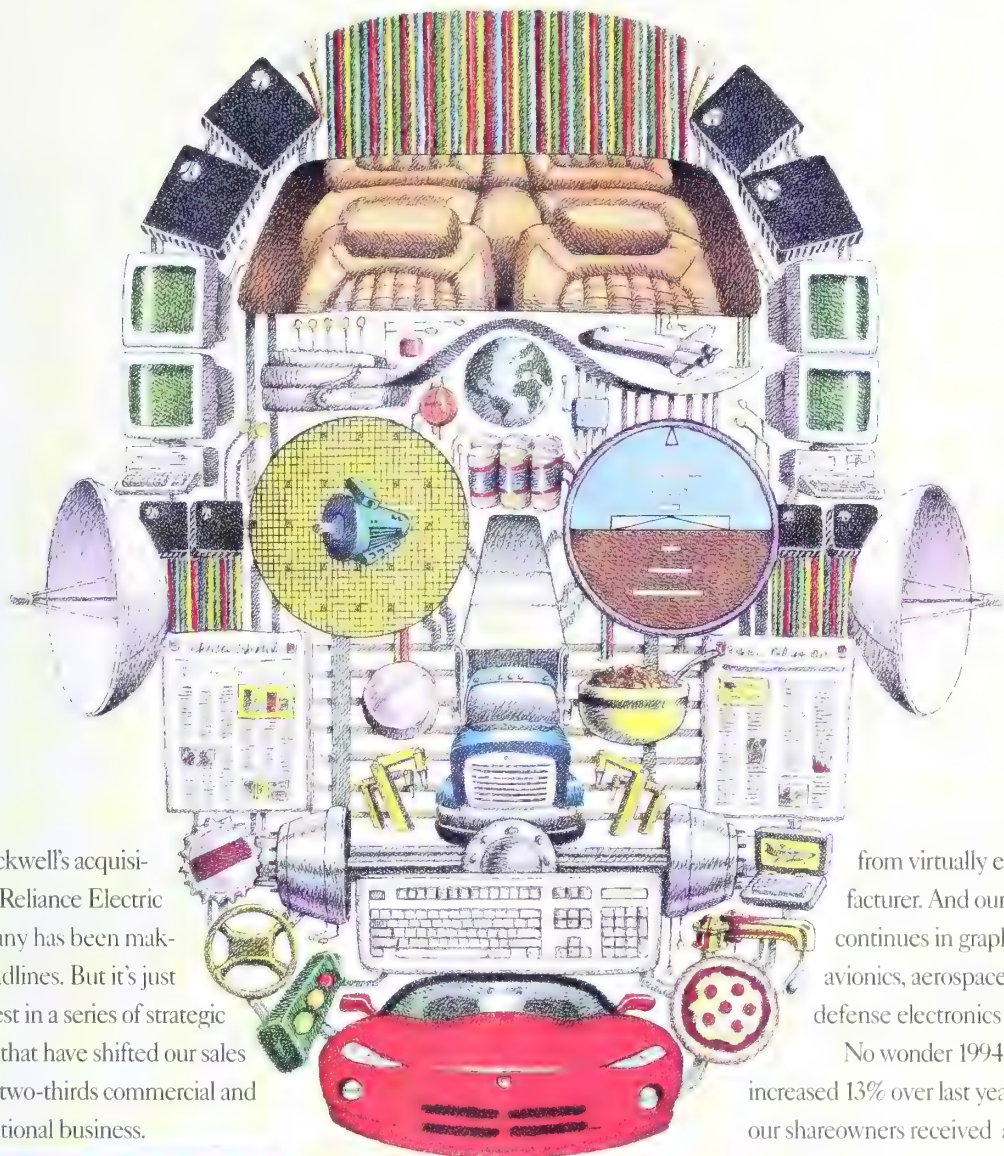
TANGLED WEB. It is a mistake for Republicans to focus on minor modifications when it is easier to abolish the current tax system than improve it. Under current budgetary rules, tax changes require expenditure changes. Steps cannot be taken to make the tax system fairer to families with children or improve economic incentives unless expenditures are cut commensurately. But the spending cuts pit organized interest groups against unorganized families with children. These tax and spending changes could be pushed through, but the effort required would be enormous for a minor improvement.

The current U.S. tax system is the worst imaginable. Even its supporters concede that its purpose is to appease envy by penalizing success, but in fact the tax system worsens income inequality. Progressive tax rates and multiple taxation of saving, together with the payroll tax, make it all but impossible for any but the most able, determined, and lucky to break through to affluence.

The left will scream about any alternative to the progressive income tax because it believes that the purpose of taxation is to achieve equality by leveling differences in success. To the left's way of thinking, only the government should have any money, and everyone should be equally dependent on Washington. The left, however, was smashed in the last election, an indication that voters are fed up with the handicapping imposed by the current tax system.

There is no more hated institution in American life than the Internal Revenue Service. Once people realize that under Ways & Means Chairman Archer's system, they would no longer have to report their income or have any relationship with the IRS, support for his proposal will be overwhelming. To free Americans from the fear of frame-ups and arbitrary rulings; seizures of property; penalties; and interest would be the greatest act of emancipation since 1865.

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Service and Support

BY GENE KORETZ

INSIDERS ARE MIGHTY BULLISH

They're buying their own stocks

The stock market was a nonstarter in 1994, but not purchases by executives of stocks in their own companies. *Vickers Weekly Insider Report*, which keeps tabs on insider trading, notes that its eight-week Sell/Buy ratio turned highly optimistic in the middle of last year, slipped a bit in the fall, and is now giving off strong optimistic signals again.

History indicates that whenever the ratio falls below 2.25, a rising market usually follows. The ratio is now hovering at about 0.94, compared with 1.77 at the start of 1995.

In the 20 years *Vickers* has tracked insider trading, the ratio dipped below 1.1 only six times prior to 1994, and the average rise in the Dow Jones industrial average 12 months later was 23%. In 1994, it moved below 1.1 in June and has now fallen even further.

THE FOREIGN CAPACITY MYTH

It may not temper U.S. inflation

One of the oft-cited arguments against a coming pickup in inflation is that lower capacity use overseas will continue to keep a lid on U.S. import prices and thus reduce inflationary pressures. As a study by economist James A. Orr of the Federal Reserve Bank of New York indicates, domestic prices of manufactured goods in other industrial countries have trailed the rise in U.S. prices since 1990 by as much as 10% in the case of Japan. And import prices of such goods did indeed rise less than U.S. prices through mid-1994.

The problem, notes Orr, is that the effects of lower inflation abroad were substantially altered by currency movements. The dollar prices of manufactured imports from Western Europe and Canada actually fell by 7% relative to U.S. prices between 1990 and mid-1994, but that was mainly because the dollar appreciated against their currencies. At the same time, prices of Japanese imports rose by 6% more than U.S. products because the dollar depreciated by 17% against the yen.

The upshot of these trends in which rising dollar prices of Japanese products offset lower prices of imports from Canada and Europe is that U.S. import prices overall grew only 1% less than U.S.

IMPORT PRICES ARE SURGING



domestic prices. Without currency shifts, however, Orr calculates that U.S. import prices would have trailed domestic inflation by a hefty 5%.

In other words, in a world of shifting exchange rates, spare capacity overseas may exert little or no downward pressure on U.S. prices. Indeed, import inflation has already picked up substantially in recent months—a trend that rising capacity use overseas in coming years may well exacerbate.

DRINK UP, IT'S AN EXPANSION

Booze flows when income grows

As tipplers will tell you, booze can ease many pains—including economic woes. Nevertheless, a new National Bureau of Economic Research study by economist Christopher J. Ruhm concludes that alcohol consumption and vehicle fatality rates (often due to drunken driving) are procyclical rather than countercyclical. That is, they rise when the economy improves and slow or decline when it worsens.

Using data for 48 states from 1975 through 1988, Ruhm found that a one-point rise in the percentage of people employed in a state boosted liquor demand by about 0.8% and a \$1,000 rise in per capita personal income (1987 dollars) raised consumption by about 1.2%. Traffic fatalities also rose. On the other hand, rising joblessness and falling real income were associated with declining consumption and fewer fatalities.

Ruhm also found that drinking of distilled spirits was roughly twice as sensitive to changes in the economy as consumption of beer or wine—a finding in line with its higher average cost. "While some people may drink more in times of economic distress," he says, "for most people, this reaction is apparently more than offset by the constraints of lower incomes."

CHINA VS. THE U.S.: BEIJING BLINKS

Chinese exporters need America

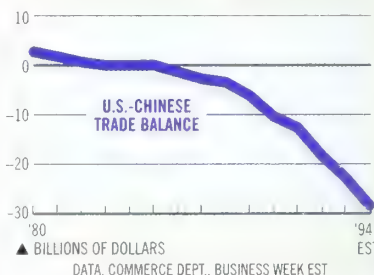
Many observers believe the current dispute between the U.S. and China over Chinese piracy of U.S. movies, software, and intellectual property will be resolved with a compromise, if only because both sides have so much to lose. Indeed, the Chinese have already acceded to many U.S. demands, at least on paper.

Still the U.S. is hanging tough. It is insisting on concrete actions, both to open Chinese markets more fully to U.S. film, music, software, and publishing industries and to crack down on Chinese factories that pirate such products for sale within China and abroad.

A major reason for America's tough stance is the skyrocketing U.S. trade deficit with China. Since 1988, U.S. imports from China have shot up like a Chinese firecracker, climbing by over \$25 billion, to an estimated \$39 billion. But U.S. exports to China have risen by only \$3 billion to \$4 billion, and in recent months, they have actually fallen below year-earlier levels. As a result, the U.S. trade deficit with China is now second only to that with Japan and accounts for roughly 20% of America's total trade deficit.

Faced with a ballooning trade deficit, China last year managed to move from a shortfall of \$12.2 billion in 1993 to a trade surplus of \$5 billion—while grow-

AMERICA'S DEEPENING TRADE DEFICIT WITH CHINA



ing at more than an 11% pace. Without American demand, which consumes more than a third of China's exports, this impressive turnaround would have been impossible.

Thus, it is China rather than the U.S. that has mainly profited from Sino-American trade so far. And as the U.S. demands a level playing field, it finds its strongest ammunition in the heavily one-sided trade data.

WHAT'S MIRIAM BERGMANN'S SECRET TO CULTIVATING AWARD-WINNING RIGOLETTO DAHLIAS?



(IT AIN'T THE WATER.)

Sure, they need the moisture, but the little darlings really perk up to the classics," said Miriam.

It occurred to her at the San Jose Center for Performing Arts. She made the intuitive leap during a particularly stirring passage of Stravinski's Rites of Spring. Miriam, and her dahlias, can be a lesson to us all: a community endowed with a healthy portion of the Arts enriches the lives of all who live there.

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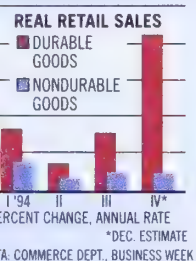
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DON'T BE FOOLED. THE ECONOMY IS STILL TOO HOT FOR THE FED

U.S. ECONOMY

Every good mystery has a few red herrings scattered among relevant evidence. In the search to pinpoint the arrival of a slower economy, the latest data throw out conflicting clues. In December, industrial output was exceedingly strong, but retail sales were a big disappointment. Which is the real McCoy and which is the MacGuffin? Deciding which indicators give a true picture of the economy is crucial for the Federal Reserve Board right now. After hiking interest rates six times in 1994, Fed policymakers will sit down again on Jan. 31-Feb. 1 to decide whether the economy needs yet another dose of restraint. Make no mistake: Slowing the economy is the *raison d'être* for Fed chairman Alan Greenspan & Co. They see this as the only way to hold back inflationary forces. Working with monetary policy already in a restrictive mode, reading the tea leaves now could spell trouble later on: A tightening, and the economy could stagnate.

CARS, COMPUTERS OUT: CLOTHING



That's especially true since foreign demand may well be a tad weaker this year than first thought. That's because the devaluation of the Mexican peso is reverberating through other economies. As sell-offs in financial markets around the world show, investors are shunning high-debt, fiscally unsound countries. One result is tighter credit conditions globally that will slow growth worldwide and mute some of the expected strength in U.S. exports. Exports to Latin America accounted for about a third of U.S. export growth in 1994.

DOMESTIC DEMAND, though, that will bend this economy to a noninflationary pace. And the December report on retail sales seemed to point to a slowdown. Not surprisingly, the 0.1% drop was unexpected—the median forecast among economists was a 0.7% gain—but the Commerce Dept. also revised the November increase down sharply, from a 1.2% jump to 0.2%. The bond market rallied sharply on the retail data, and the stock markets also boomed, so the odds of another Fed rate hike seemed to lessen. But in light of December's surprisingly robust industrial activity, the retail sales report looks like a red herring. Retail sales are one of the government's most volatile indicators, and as the November revision shows, the December drop may not hold up as more retailers report in.

Moreover, a look below the surface suggests that buying for the entire quarter was pretty strong—especially for durable goods, the very sector where the Fed's rate hikes should be having an impact (chart).

Yes, demand for durable goods weakened in December—but after four months of strong buying. Building materials, furniture, and electronics got snapped up. Even after adjusting for price changes, quarterly sales at durable-goods stores shot up at an annual rate of 21%.

Retailers in the nondurable categories—from grocery stores to gas stations to restaurants—had a harder time in the fourth quarter. Department stores, in particular, had to pump up their sales volume by cutting prices during December in order to compete with discounters—increasingly, the merchant of choice in the 1990s. That means real purchases of nondurable goods rose at a modest 2.5% in the fourth quarter.

For retailers, sales promotions meant yearend profits were quite a letdown, the chief reason retailers sound so humbug about holiday sales. But for consumers, November and December sales rose 6.8% from a year ago. That's not bad, considering that 1993 receipts posted a 7% gain, a result retailers seemed quite pleased with at the time.

IS CAPACITY GETTING TOO TIGHT?



THE RESILIENCE of consumers is one reason the Fed is apt to ratchet up rates at the end of January. The Fed's latest survey of activity in each of its 12 regions, prepared for its upcoming meeting, reported that the "economic expansion remained vibrant across much of the nation."

The report also said that "the underlying momentum in consumer spending growth remained quite strong" in December and early January. Indeed, household buying last quarter appears to have boosted real gross domestic product at an annual rate of at least 4%—the third quarter in a row in which growth was 4% or better. That's a killer pace in the eyes of the Fed.

The strength in the factory sector, especially the jump in operating rates (chart), is an even tougher argument for a rate hike. The 1% surge in industrial output in December—the largest in more than two years—shows an economy headed into 1995 with plenty of momentum.

Factories alone lifted output by 1% in both November and December. For the fourth quarter, total industrial

output grew at a 5.4% annual rate, and factory production rose 7.3%—the same pace as in the first half of 1994 before any rate hikes had a chance to bite.

Like retail sales, durable goods are a key to industry's strength. Output of consumer durables was up 6.4% in the fourth quarter, and business equipment surged 11%, with a 27.2% gain in computers and office machinery.

FOR THE FED, the sharp rise in utilization rates has to be particularly worrisome. All industry used 85.4% of capacity in December. That's up from 84.7% in November and is the highest operating rate in 15 years. In primary processing, the rate rose from 89.3% in November to 90% in December, the highest in 21 years. Traditionally, an operating rate of more than 85% is one of inflation's smoking guns.

But while rising plant use suggests at least a slight pickup in inflation this year, the Fed must also factor into its policy talks the concerns that the operating rate is no longer a dependable gauge of price pressures. Many economists argue that slack capacity abroad acts as a safety valve if operating pressures become too high in the U.S. Also, businesses are using computers and other technology in an effort to boost efficiency, which increases their output capabilities.

One factor that promises to take some of the starch out of the factory sector as the year wears on is inventories.

Business inventories remained quite lean in relation to sales in November, but that reflected skimpy inventories at the manufacturing level. Inventories in manufacturing, wholesaling, and retailing rose 0.7% in November against a 1% increase in business sales.

For retailers alone, however, inventories have been growing faster than sales for three of the past four months. The imbalance is especially acute outside of car dealers. The ratio of nonauto inventories to sales in November rose to the highest level in 8½ years (chart). And after December's soft sales, retailers may have started 1995 with more goods than they wanted, making vendors skittish about reordering in 1995.

Although foreign producers will take some of the hit, domestic manufacturers will feel some drag as well.

Right now, though, the overwhelming body of evidence points to a stubbornly strong economy headed into 1995 with considerably more momentum than the Fed wants. To be sure, Fed tightening will slow the economy this year, but not even the central bank can be sure when that will happen. That's why the first rate hike of 1995 may not be the last.

RETAILERS LOOK A BIT OVERSTOCKED



EUROPE

THE FRANC FORT IS UNDER SIEGE

The French economy begins 1995 amid excellent prospects for solid, noninflationary growth. The same for Germany. So why has France's "strong franc" been losing ground to the German mark?

It's hard to make a rational case for franc weakness. Most analysts expect French economic growth, led by exports and capital spending, to accelerate this year to between 3% and 3½% from an expected 2.4% in 1994. Strong exports will help France maintain its trade surplus.

And consumer inflation, which dipped to a 40-year low of 1.6% in November, will stay down. Slack labor markets—November joblessness held at a near-record 12.6%—

will mute wage and price pressures and keep inflation near the Bank of France's 2% goal.

But currency markets aren't always rational. Right now, the franc is the victim of Eurocurrency turmoil (page 46). Portfolio

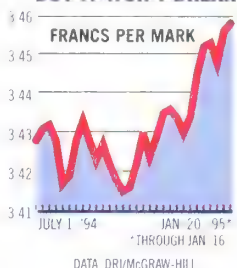
shifts out of swooning currencies have favored the safety of the mark at the franc's expense. Also, the political uncertainty surrounding the French presidential elections this spring has made the markets jittery—perhaps overly so.

Neither of the key candidates—current Prime Minister Edouard Balladur and Jacques Chirac—is likely to tamper with the *franc fort* policy of linking France's monetary

policy to Germany's, and both have endorsed fiscal moderation as a needed step toward an eventual European monetary union. Moreover, Balladur, the financial markets' favorite candidate, leads all the polls.

One stumbling block for the franc could be the French government's slower pace of fiscal improvement. The 1994 fiscal deficit stood at 5.7% of gross domestic product vs. Germany's 2.7%. European markets are increasingly rewarding those countries that show the political will to get their finances in order while punishing those that do not. That means maintaining the *franc fort* will not only demand higher interest rates but it may also require tax hikes at a time when domestic demand is already limited by chronic unemployment.

THE FRANC BENDS, BUT IT WON'T BREAK

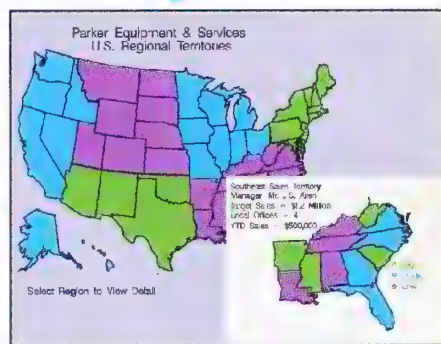
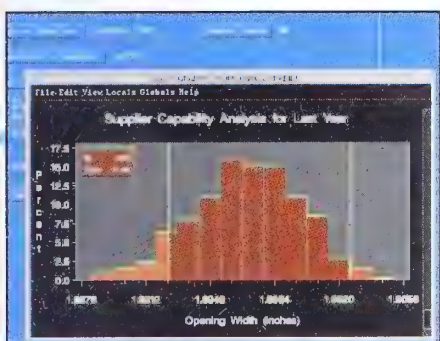


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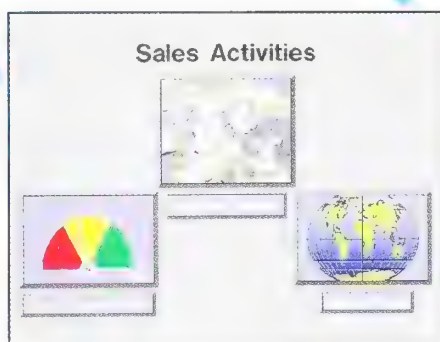


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BLOWUP AT BRIDGESTONE



The tiremaker that can say no has drawn Clinton's ire

Thunder" Thornton, a machine operator at Bridgestone/Firestone Inc.'s tire plant in Des Moines, figured from the start it would be a long strike. "They were out to starve us to death, and they've done a pretty good job of it," says the 31-year company veteran.

The six-month standoff between Bridgestone and the United Rubber Workers (URW) indeed has turned into an acrimonious confrontation. On Jan. 18, after months of secret talks—and two weeks after the company revealed it had hired permanent replacement workers—both sides sat down with federal mediators. But Bridgestone officials indicated even before the meeting began that they weren't likely to rehire all the striking workers, and union officials

said their prospects looked bleak.

If this were just a strike, the matter might end there: Big Labor, representing just 11% of America's private-sector workers, rarely gets front-page treatment anymore. But the Bridgestone battle has spiraled into a remarkable political spat, replete with tense diplomatic dialogue and high-level snubs.

The Clinton Administration has seized on the dispute, finding in the rubber workers a vehicle to score points with organized labor and, as well, with conservative Democrats and suburban independents. The fact that the employer is a Japanese company, at a time when trade relations with Tokyo are faltering badly, hasn't hurt. For Clinton, says adviser Paul E. Begala, the strike "has a special saliency. It doesn't matter if you are in a labor union. It's a matter of common decency." Translation: This one can win votes.

The President has publicly criticized Bridgestone's January hiring of 2,300 permanent replacement workers. Labor Secretary Robert B. Reich complained loudly after the company's top U.S. official declined to meet with him about the issue. And at a formal White House luncheon during the Japanese Prime Min-

ister Tomiichi Murayama's January visit, Ambassador Walter F. Mondale took the highly unusual step of raising the matter with the Japanese Foreign Minister.

All this has enveloped a company that once seemed a model of management-labor cooperation. After Japan's Bridgestone Corp. bought Firestone Tire & Rubber Co. in 1988, labor relations were downright friendly. Management even allowed the URW to represent workers at a new plant.

DESTABILIZING. But the coziness vanished after the company posted a total of \$1 billion in losses by 1992, and after the ascension of cost-cutter Yoichiro Kaizaki to head Bridgestone/Firestone in 1991—and, later, its Japanese parent. Kaizaki, and then Masatoshi Ono, his replacement in the U.S., abandoned the cooperative relationship and girded for a showdown in April, 1994, when the labor pact was set to expire. The company padded inventory by buying more than 500,000 tires from rival Cooper Tire & Rubber Co. Bridgestone in Japan agreed to supply another 3 million tires, according to a 1993 memo from Ono that the union released. Bridgestone headquarters denies knowledge of the memo.

Armed with inventory, management

ANATOMY OF AN INTERNATIONAL INCIDENT

1993

The United Rubber Workers charge Bridgestone with organizing other tire makers to prepare for a strike, an assertion the company denies.

AUGUST

Bridgestone implements parts of its contract proposal. It operates the struck plants with salaried personnel and some new workers, though below capacity. Later, the company and the URW charge each other with unfair labor practices.

APR. 18, 1994

Labor Secretary Robert Reich, at an Oklahoma City plant, fines Bridgestone \$7.5 million for allegedly violating



safety standards. The case is now in administrative review.

APR. 23

URW contracts with major tiremakers expire. After the union settles with Goodyear in June, negotiations resume with Bridgestone. But the company refuses a "pattern" settlement, and the union rejects Bridgestone's proposal.

JULY 12



More than 4,000 workers under URW President Kenneth Coss strike five Bridgestone/Firestone factories. Reich blasts the company for its bargaining stance.

JAN. 4, 1995

Bridgestone says it has hired more than 2,000 permanent replacement workers. Reich attempts unsuccessfully to



meet with Bridgestone/Firestone CEO Masatoshi Ono.

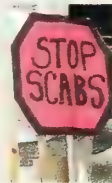
JAN. 11



Ambassador to Japan Walter Mondale tells Japanese Foreign Minister Yohei Kono at a White House state luncheon that Ono should meet with Reich.

JAN. 13

Bridgestone agrees to meet with the URW and U.S. mediators. (Ono later says he is willing to talk with Reich.) President Clinton criticizes the company for hiring replacements.



anded that the URW break with the contract it ratified in June with Goodyear Tire & Rubber Co., which called for a 16% increase over three years. In place, Bridgestone asked for 12-hour shifts, pay hikes tied to productivity gains, health co-payments, and lower hiring pay—all to overcome what it said were big cost disadvantages. The union refused. "They're trying to destabilize the entire American tire industry," says URW President Kenneth L. Coss.

On July 12, 4,200 union members walked out at five plants covered by the contract. Reich criticized Bridgestone for refusing to accept the pattern contract negotiated at Goodyear. This wasn't Bridgestone's first run-in with the Labor Secretary. In April, Reich had flown to the tiremaker's Oklahoma City plant and personally slapped the company with a \$7.5 million fine for alleged safety violations. The case is still pending.

A series of secret talks went nowhere in the next few months, even though

insiders say the union agreed to concessions. In the meantime, Bridgestone's stockpile, and production from its other union and nonunion factories unaffected by the strike, allowed it to keep most major customers supplied. "It's almost like the strike never existed," says Larry Morgan, chairman of Don Olson Tire & Auto Centers in Clearwater, Fla.

REBUFFED. On Jan. 4, Bridgestone announced it had hired 2,000 permanent replacements. The move struck a nerve in the Administration, which supports a law to limit employers' ability to replace strikers for good. Reich, who has intervened in six major strikes, tried to speak with Ono, and with Kaizaki, hoping to get the two sides talking again. Instead of quietly agreeing, Bridgestone rebuffed Reich, saying Ono was unavailable and offering its labor chief instead.

An angry Reich complained to Clinton, and the President seized the chance to curry favor with Labor. Though his support of the striker replacement bill

last year was halfhearted, Clinton still wants to appeal to workers alienated by his support for issues such as NAFTA.

At the White House luncheon on Jan. 11, Mondale told Japanese Foreign Minister Yohei Kono that Ono should speak with Reich. Two days later, Clinton himself weighed in. In a statement, he said he had "long supported legislation to prevent companies from permanently replacing their striking workers. Now Bridgestone/Firestone's use of permanent replacements shows exactly why this protection is necessary."

Bridgestone had alienated other U.S. policymakers as well. A group of four Democrats led by Senator Paul Simon (D-Ill.) tried several times to intervene in the dispute. After a November visit to Japan's U.S. Ambassador came to naught, the Senators got Senate leaders to give Murayama a letter protesting Bridgestone's actions. Simon also raised the issue with the Prime Minister when he visited the Senate floor on Jan. 11. Fi-

The Administration sees worker replacement as an issue that can win back labor support lost over NAFTA

nally, the next day, Ono said the company would meet with the union. And Ono agreed to meet Jan. 23 with Reich, although there's no evidence that Japanese officials pressured him to act.

New talks may not help. Bridgestone already has said some strikers will lose their jobs, making it politically difficult for the URW to return to work. The company's new 12-hour shifts may require a

larger workforce. But with just 800 union line-crossers and 300 more replacements hired after the first 2,000, Bridgestone says it's running the struck plants at 70% or more of normal production.

Indeed, Bridgestone likely will win. And to Clinton's attack, it responds: "Our offer to the URW is in keeping with Mr. Clinton's stated goals of U.S. economic growth and American compet-

itiveness in the global marketplace." It sounds smug. Still, U.S. officials vow to keep up their attack, even in a losing cause. "We plan to keep the pressure up on both sides," vows Steven Rosenthal, an assistant to Reich. If so, this international incident may be far from over.

By Zachary Schiller in Cleveland, with Douglas Harbrecht in Washington and bureau reports

THE WHITE HOUSE

AND NOW, THE STATE OF BILL CLINTON SPEECH

Can he find a message that gets him on the comeback trail?

The worst-kept secret in Washington is that Bill Clinton is engaged in a massive bout of soul-searching. In recent weeks, he has huddled with politicians, motivational gurus, and policy wonks. All this thrashing underscores an urgent concern: How can a President who led his party to its worst drubbing in 40 years and has since been overshadowed by GOP quote machines such as House Speaker Newt Gingrich reassert control of the public dialogue?

The answer will come on Jan. 24, when the President delivers his State of the Union address. He hopes to use this forum to claw back into the game with a three-pronged strategy: pushing popular programs under his Middle-Class Bill of Rights, attacking Republicans as extremists, and addressing Americans' moral yearning by speaking on values and the need for greater community.

GOOD NEWS. Although critics may deride Clinton's fitness to lead a moral crusade, there's no question about his devotion to populism. In the 1992 race, he tapped into middle-class jitters about the global economy, and he's prepared to renew the theme in his bid for reelection. "He's returning to his roots," says a White House adviser. Apparently, the new tack is helping. According to a Jan. 11-12 Time-CNN poll, 49% of the public approves of the job Clinton is doing, up from 41% in early December.

That's good news for the White House. For weeks, Presidential advisers have debated whether their man should move left, toward his base, or jump right. Instead, they came up with a synthesis that promotes "web issues," such as job training and crime fighting. A Clinton adviser describes these as "issues that stitch folks back together again" by appealing to core Democratic constitu-

encies and suburban independents.

One key web theme is education. The issue has scored well in polls, persuading Clinton to propose a tax break of up to \$10,000 a year to help middle-class parents pay for college. Another web



POPULIST Clinton, sharing the stage on Martin Luther King Day in Los Angeles, is renewing his image as a working-class hero. Practically unnoticed in all the Newt hoopla, the President's ratings are up

idea is the Clintonites' call to streamline government, which they hope will appeal more to voters than the GOP's proposals for shock treatment. After the State of the Union, Clinton plans to hit the hustings to hawk his latest Reinventing Government ideas, among them

a scheme to shrink the Interior Dept.

Clinton also will resurrect his campaign theme of a New Covenant government that provides opportunities in return for responsibility. In this vein, welfare mothers will receive aid if they work, and workers can get grants if they improve their job skills.

TAKING COURAGE. Another tactical shift: Clinton mainly has sought common ground with Republicans since the elections, but lately he has started to carefully pick fights. On Jan. 16, he lashed out at Gingrich for vowing to end a pet Clinton program: AmeriCorps, which gives college loans to students

who do community work. Aides also plan increasingly to attack Republicans on issues such as repeal of the assault weapons ban while painting them as heartless Grinches who aim to throw welfare kids onto park benches. Meanwhile, they're hoping for more GOP pratfalls, such as Gingrich's stumble over his \$4.5 million book contract. "The more he's discredited, the more his agenda suffers," says a gleeful White House aide.

Of course, that's a problem for Clinton as well. Republicans plan to make plenty more hay over the Whitewater scandal and Paula Jones's harassment allegations. Nor can Clinton depend on Republicans slipping on every banana peel. Moreover, he undermines his political standing with chronic vacillation. But having Newt in his face may be just what it takes for Clinton to finally learn how to stick to the script.

By Susan B. Garland, with Douglas Harbrecht, in Washington



SECTION '96

THE GENE McCARTHY OF THE WAR ON ABORTION?

Democrat Robert Casey is pro-life—and on a crusade

outgoing Pennsylvania Governor Robert P. Casey doesn't let go easily. He lost three gubernatorial races at least partly because another candidate had the same name—before finally triumphed in 1986. Then, last year, he nearly died of a rare liver disease. Only a risky heart-and-liver transplant saved his life—and eventually allowed him to reassume power.

Still frail after his ordeal, the two-term governor would seem due for some respite. Instead, Casey, 63, is embarking on a campaign to open up a space in the Democratic Party for religious and pro-life candidates. To rebuild what he views as a repressed wing of the party, Casey says he's considering a run against President Clinton next year for the Democratic nomination. "The Democratic Party is viewed as a launchpad for assaults on basic American values," he gripes on a plane from Harrisburg to Scranton on Jan. 16, his last day as governor. "Anyone who has my perspective is silenced."

NG BLOC. Casey likely would have a chance of winning the Presidency, but he could make life miserable for Clinton. The nightmare scenario for the president: Casey could attract millions of voters in the key right-wing swing bloc within the Democratic Party. And as Republican Patrick J. Buchanan did to President Bush in 1992 and Eugene McCarthy did to Lyndon Johnson in 1968, Casey could shine a spotlight on a vulner-

able President's weaknesses in the early Presidential primaries. If Casey can't win, he might create an opening for a stronger Democratic challenger, much as McCarthy did for Robert F. Kennedy.

Contrary to conventional wisdom, Casey believes the Democrats lost last November's elections on moral issues. He maintains that a clique of leftists around Clinton are bent on driving values and God out of the American debate.

GRUMPY GADFLY "The Democratic Party is viewed as a launching pad for assaults on basic American values. Anyone who has my perspective is silenced" — ROBERT CASEY

But pointing to references to God in the Declaration of Independence and recalling Franklin Roosevelt leading the nation in prayer on D day, Casey says: "That's who we are, a religious people whose institutions presuppose a supreme being." Such remarks won him thunderous ovations when—as the lone Democrat—he spoke to a Christian Coalition gathering last fall. He's not fund-raising yet, but he probably will get strong support from such groups if he challenges Clinton.

But if Casey is conservative on values, he sees government as vigorously activist. He boasts of spending more on clean water than any governor in the country,

GOING HOME: Casey has been battling Clinton since the 1992 convention

providing health insurance for 40,000 poor children, reviving steel mills—all while leaving the state with a budget surplus. These programs, along with sympathy following his surgery, make Casey the most popular outgoing governor in three decades, even if his tough environmental policies and a \$3 billion tax hike in 1991 made him few friends in business.

Clinton and Casey have been battling since the 1992 Democratic Convention. Casey wanted to address the gathering, but he refused to support Clinton first. Clinton's team denied him the spot. Further, says Casey, they invited Kathy Taylor, a pro-choice Pennsylvania Republican who had supported his opponent two years earlier, to speak. "They rubbed my nose in it," says Casey, who never did endorse Clinton.

STRONG HEART. As Clinton marched on to the White House, Casey's star dimmed. He grew thinner and weaker, his liver disease apparently killing him. But in June, 1993, surgeons at the University of Pittsburgh Medical Center performed a successful double transplant.

Barred from running for a third term, Casey focused on a national pro-life agenda. Last fall, with his recovery well along, he infuriated state Democrats by refusing to support pro-choice candidates, including his lieutenant governor, Mark S. Singel, and Harris Wofford, whom he appointed to replace late Republican Senator John Heinz.

Early this month, Casey's surgeons assured him his new organs are doing well. He now takes a single anti-rejection pill a day, and doctors say his life

expectancy is normal. "Everything looks good. His heart is stronger now than when it was put in," says Dr. John Fung, one of his surgeons.

Casey, his wife, Ellen, and their eight children are mulling whether he should make a serious run for the White House. "Somebody's got to do it," he says. He knows his health will be an issue. But even if he can't mount a Bobby Kennedy-style challenge to Clinton, a Casey candidacy still could be as damaging as those of McCarthy and Buchanan.

By Stephen Baker on board the governor's plane, with Richard S. Dunham in Washington

TAXES

SO MANY TAX-CUTTERS, SO LITTLE ROOM TO MANEUVER

Those big reform plans may boil down to a modest reduction

On paper, 1995 looks like the year of the Big Tax Cut. The legislative hopper is already bulging with bills to cut levies on the middle class, on savings and investment, and on capital gains. Other provisions would repeal the so-called marriage tax penalty, roll back tax hikes on the elderly, help build savings for college tuition, and even scrap the entire income-tax code and replace it with a single rate.

But don't start ordering the expensive leather seats on the new car of your dreams just yet. To get to the promised land of tax reduction, Congress and the White House must first cross the narrow bridge of spending cuts. And both parties have agreed that every dollar of proposed tax cuts be offset by a dollar in spending cuts. That pledge may block Americans from getting the cornucopia of goodies promised in the GOP Contract With America or President Clinton's Middle Class Bill of Rights.

The likely outcome: Both sides will

have to scale back their proposed cuts and focus on the most popular items—breaks for college tuition, retirement savings, and capital gains. Meanwhile, even ardent supporters acknowledge that flat-tax bills and other tax-reform proposals may not get serious consideration until after the 1996 elections.

At least the debate won't be dull. "We're going to see every possible gimmick to reduce the deficit and offset tax cuts that you can think of, and huge disagreements on baselines, asset sales, and accounting all year long," predicts Susan Tanaka, vice-president of the Committee for a Responsible Federal Budget, a bipartisan group that wants to eliminate the deficit.

SERIOUS DRAIN. Despite detailed plans for tax cuts, neither party is ready to go public with equally explicit spending cuts. And no wonder. To do everything the GOP Contract calls for—cutting taxes, raising defense spending, and balancing the budget by 2002—Congress will have

to find more than \$1.4 trillion in spending cuts in seven years. Clinton's "family" tax-cut plan is cheaper than the GOP version—just \$60 billion over five years vs. \$197 billion for the Republican plan—but the White House hasn't yet specified most of its offsetting spending trims.

Fortunately, some of the most politically popular items are also the cheapest—at least in the short term. The GOP's \$500-per-child tax credit for families earning under \$200,000 a year would cost a colossal \$107.2 billion over five years, but its capital-gains cut would cost only \$57.5 billion, according to the Treasury Dept. An even better bargain is the GOP's proposal for expanded individual retirement accounts, which would cost a mere \$1.5 billion over five years. The Administration's IRA plan would cost just \$3.7 billion. And Clinton's proposed deduction of up to \$10,000 for college and other postsecondary education would cost \$20.6 billion over five years. White House polls show the school deduction to be Clinton's most popular idea by far.

Yet even these lesser tax cuts cause a far larger revenue loss once they are fully phased in. For example, excluding 50% of capital gains from taxes and indexing gains for inflation triples the cost, to \$170.4 billion, over 10 years.

Meanwhile, business frets that Congress may drop items from its wish list, such as the capital-gains tax cut. The

SLASH, FLATTEN, SIMPLIFY!

Major tax-cut and reform measures likely to be considered by Congress

CONTRACT WITH AMERICA This GOP measure would offer such tax cuts as a \$500-per-child credit for most families, a 50% capital-gains exclusion, and an "American Dream Savings Account" to help fund retirement, medical, or education expenses. The marriage penalty and the 1993 hike on Social Security income would be rolled back.

CHANCES OF PASSAGE House approval likely, but the Senate may scale back to avoid increasing the deficit.

MIDDLE CLASS BILL OF RIGHTS The Clinton plan would include a \$500-per-child credit for some families, a \$10,000 deduction for expenses for postsecondary training and education, and expanded IRAs.

CHANCES OF PASSAGE Cheaper than the Contract, but won't get GOP backing.

FLAT TAX Representative Dick Armey (R-Tex.) wants to replace the current income tax on businesses and individuals with a flat 17% rate. Representative Richard A. Gephardt (D-Mo.) also has a flat-tax plan.

CHANCES OF PASSAGE Slim in the short run.

SAVINGS EXEMPT TAX Senators Sam Nunn (D-Ga.) and Pete V. Domenici (R-N.M.) want to replace the individual and corporate federal income tax and a portion of the Social Security payroll tax. Business would subtract from domestic sales all purchases from other businesses and pay a 7.1% rate. For individuals, savings would be deducted from income.

CHANCES OF PASSAGE Very slim.



S. Chamber of Commerce is encouraging both parties to drop plans for tax cuts for children. Then, it figures, Clinton could swallow a capital-gains cut in return for his college-tuition deduction. Lobbyists also hope to persuade Treasury and Congress to recalculate the effect of a capital-gains cut to show it does not drain much revenue. "It would unlock so much capital and have such an impact on savings and investment, it could be a wash over five years," insists Mark A. Bloomfield, president of the American Council for Capital Formation, a manufacturers' advocacy group. But many economists doubt that tax cuts of such magnitude are wise with the deficit expected to hit \$322 billion in 1995. "The real issue ought to be tax reform, because we can't possibly afford tax cuts," says Lawrence H. White, chief economist at Washington's Economic Strategy Institute.

Although tax reform makes far more economic sense than tax cuts, any overhaul of the code faces huge hurdles—high cost and the enormity of the proposals. House Majority Leader Richard Armey (R-Tex.) has proposed the most popular reform: a flat 17% income tax rate for individual wages and pensions and business cash flow. A family of four, for example, eventually would fill a 1040 postcard by subtracting from their wages a \$26,200 personal allowance and a \$10,600 dependent deduction. No withholding and no taxes on savings, inheritance, or capital gains.

HAUL. The concept even has bipartisan appeal. House Minority Leader Charles A. Gephhardt (D-Mo.) says he is drafting his own flat tax of 10% or 12%. "If you have two people as unlike Gephhardt and Armey talking about it, the chances for passage are pretty good," says David Keating, executive director of the National Taxpayers Union. But even Keating admits that such a change isn't likely before 1997, when a GOP Presidential candidate raises the issue's visibility. And Armey admits his plan would produce a shortfall of \$186 billion in the first year, while the Treasury Dept. pegs the loss at a catastrophic \$186 billion a year after full phase-in. Cost aside, experience shows that large-scale tax reform, such as the overhaul of 1986, requires a long process of education and compromise.

Still, it won't hurt the tax-reduction cause that the 1996 Presidential election is looming. Clinton is less likely to risk voters' wrath by vetoing a tax-cut now. Yet polls show that much as public hates income taxes, it hates the federal budget deficit even more. The message from voters: Make 1995 the year of the Big Spending Cut.

By Paul Magnusson in Washington

FUNDS

WILL CalPERS LEAD A PARADE DOWN WALL STREET?

Other pension funds could follow its big shift into equities

Call it a shot in the arm for stocks. Last month, the California Public Employees' Retirement System (CalPERS) quietly voted to increase its equity investments from 49% of its \$80 billion fund to 63%—well above the level of its most aggressive peers. Bond investments are expected to drop to 30% from 43%. That huge swing represents an \$11 billion vote of confidence in the stock market.

For now, CalPERS' big bet makes it one of the most aggressive pension funds around. According to Greenwich Associates Inc., the average public fund has just 49% of its assets in equities. In time, CalPERS should surpass even the equity allocation of less conservative corporate funds, which on average keep 60% of their funds in stocks. "It's a very gutsy move," says Steven H. Nagourney, chief global strategist for Lehman

Brothers Inc. "They're setting up their portfolio for a new world order."

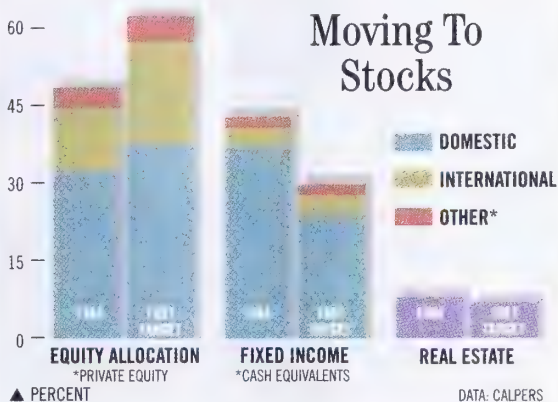
NEW VIEW. The force behind the bold move: Sheryl Pressler, CalPERS' new chief investment officer. Hired last spring from McDonnell Douglas Corp., she brings strategies from the corporate world to the state fund. The new CIO's investment plan was supported by reports from two well-regarded consultants, Wilshire Associates Inc. and Pension Consult-

ing Alliance. Neither returned calls for comment.

While CalPERS is hiking its allocation in domestic stocks, the fund's percentage of international stocks is getting the biggest boost. CalPERS aims to have foreign equities account for 20% of assets by 1997, from 12% today—far higher even than most corporate investors. Wilshire Associates, in an October memorandum, recommended that CalPERS invest in South Africa and Korea. "Wherever markets decline, we will be purchasing," says Morrill. Some 20 investment managers, among them Nomura Capital Management Inc. and State Street Global Advisors, advise the fund on international equities.

For pension funds with shorter investment horizons, mimicking CalPERS' higher-risk move may not be wise. But for funds with long-term horizons, the increased returns from equities should more than outweigh increased risks. "By the time everyone else catches on, CalPERS' returns will be much higher," says Lehman's Nagourney. And that would put CalPERS even further ahead of the pack.

By Suzanne Woolley in New York, with Eric Schine in Los Angeles



The objective is simple: higher long-term returns. By cutting back on fixed income and loading up on domestic and international stocks, CalPERS figures it can increase its return by about \$800 million a year. For the 12 months ended on Sept. 30, CalPERS' total return on assets was 0.7%; the average for public funds in that period was -0.6%, according to researcher Callan Associates Inc. "It's an opportunity for us to use our size to enhance diversification and get a better return," says Kevin Morrill, administrative manager of CalPERS' investment office.

The change won't take place overnight. The pension fund plans to make steady investments in equities over the next three years using a technique called dollar-cost averaging and plans to buy on market dips. Even so, CalPERS' action seems likely to spark imitators in the normally staid public-pension world. "Inevitably, others are going to say that this is significant, let's find out why they're doing it and see if we should do something similar," says D. Don Ezra, managing director at retirement consultant Frank Russell Co. "At the least, it ought to prompt some thinking."

COMMENTARY

By Mike McNamee

A MINIMUM-WAGE HIKE SPELLS MAXIMUM DAMAGE

When Labor Secretary Robert B. Reich in early January revived the idea of raising the minimum wage, he set a rhetorical trap for Republicans—and House Majority Leader Richard K. Armey (R-Tex.) quickly took the bait. The minimum wage shouldn't be increased, Armey said, it should be eliminated, because it harms both the economy and the poor. The exchange broadcast exactly the message the Clinton Administration wants to send: compassionate Democrats up against heartless Republicans.

Trouble is, Armey's right. The preponderance of economic evidence still holds that the minimum wage keeps low-skill, low-productivity workers from getting the jobs they need. More important, new research shows that raising the minimum wage hurts exactly those people the Clintonites are trying to help. It tempts more teenagers to drop out of school. And it raises the barriers that keep welfare recipients from finding work. When it comes to fighting poverty, Clinton should turn to a more effective weapon: the Earned Income Tax Credit.

FAULTY MODEL. Reich's call for a higher minimum wage—the White House is likely to propose raising it from \$4.25 an hour to \$5—leans on studies showing that boosting the minimum wage in 1990 and '91 didn't put a crimp in employment. In fact, Princeton University economists David Card and Alan B. Krueger found that New Jersey fast-food stores hired more workers after the state raised its minimum to \$5.05 in 1992. During the same period, employment fell at franchises in neighboring Pennsylvania, where the wage remained at \$4.25.

Card and Krueger—now Reich's chief economist—argue that low-

wage employers can fill vacant jobs and retain more productive workers when a higher minimum forces them to pay more. "The Econ 101 model of the labor market doesn't apply here," says Card.

But don't count out Econ 101 yet. In a study of dozens of federal and state minimum-wage hikes since the 1970s, David Neumark of Michigan State University found that total employment consistently dropped by 1% to 2% for every 10% rise in the mini-

that when their states raised the minimum wage, mothers on welfare stayed on the dole an average of 19.5 months, six months longer than mothers whose states didn't impose an increase.

EXPENSIVE MEDICINE. A minimum-wage hike does help some poor workers—but it's an expensive way to attack poverty. Of the \$9.7 billion cost of a 75¢ hike, only about one-quarter—\$2.7 billion—would go to poor or near-poor households, says



A higher
minimum
wage means
more dropouts,
displaced poor
workers, and
help for the
not-so-needy

um. Texas A&M University economist Finis R. Welch compared job data from 1989 and 1992 and found that employment fell most steeply among the groups most likely to be affected by the 1990-91 minimum-wage increases, such as teenagers or high school dropouts.

A 2% drop may not sound like much—except that those losses are concentrated among poor, low-skilled workers. And teenagers, Neumark finds, face a double whammy. Higher minimums tempt high school students to sacrifice education and long-run income by dropping out and taking jobs. And the new entrants push aside less educated working teens—who end up with neither schooling nor jobs.

Welfare mothers also suffer. University of Wisconsin poverty researcher Peter D. Brandon has found

Syracuse University economist Richard V. Burkhauser. A bigger chunk—\$3.3 billion—would line the pockets of spouses or teenagers in families with incomes above \$43,000.

With the GOP in control of Congress, Reich has probably missed his opportunity to win a minimum-wage hike. Instead, he should follow up on Clinton's 1993 strategy of raising the Earned Income Tax Credit. Thanks to the credit, low-income workers with two children have an effective minimum wage of \$5.78 this year. The EITC costs a lot—\$16 billion a year—but nearly all the money goes to the poor. And studies show it actually boosts work among welfare recipients. Unlike the minimum wage, the EITC is an antipoverty program that works.

McNamee covers social policy.

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CHIPS

INTEL TAKES A BULLET —AND BARELY BREAKS STRIDE

Despite the hit from the Pentium bug, '94 revenues are up 31%

Not a terrific way to start the year. On Jan. 17, Intel Corp. detailed the damage from the public-relations nightmare surrounding an obscure bug in its flagship Pentium chip: a \$475 million charge to fourth-quarter earnings to account for the costs of replacing and writing off flawed chips. A few days before, Intel abandoned an eight-year legal battle with archrival Advanced Micro Devices Inc.—a surprise win for AMD.

Is Intel losing its edge? Don't bet on it. The hit from its Pentium fiasco was unexpectedly big—at least 15% higher than analysts had anticipated—and the charge drove fourth-quarter profits down 37% from a year earlier, to \$372 million. But virtually in the same breath, Intel reported that Pentium sales had doubled from the third to the fourth quarter, helping lift 1994 revenues 31%, to \$11.5 billion. In coming weeks, the world's largest chipmaker will unleash a barrage of price cuts and new chips. And it is spending considerably more than ever to build new factories. Says John Bourgoyn, AMD's vice-

president for microprocessor products: "I don't see Intel becoming any less tough or less aggressive."

On Feb. 1, sources say, Intel will drop prices on some Pentium chips by as much as 45%. That, it hopes, will spur more PC buyers to choose the proprietary Pentium over older 486 chips, which six other companies also make. And on Feb. 16, Intel will up the ante by unveiling technical details of its next-generation microprocessor, code-named P6. The P6 aims to leapfrog Pentium

DREAM TEAM: The next-generation P6 chip is twice as fast as Pentium

wannabes due out around the same time this summer. Vows Intel Chief Operating Officer Craig R. Barrett: "We plan to be just as aggressive on the technical front as we've always been."

They have to be. For many rivals and customers, the Pentium-bug debacle exposed Intel's vulnerability. More than ever before, "the Pentium issue indicates that system vendors need an alternative source," says Ronald Chwang, president of PC maker Acer America Corp., which uses Intel and AMD chips. Intel alienated big customers such as Compaq Computer Corp. and IBM last year, partly by refusing to grant price cuts on its chips; now, those companies may move to buy more of their supplies from Intel competitors such as AMD, NexGen, and Cyrix.

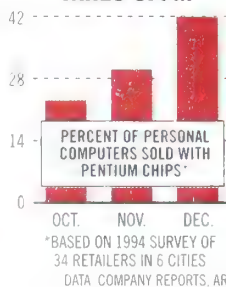
EMERGING RIVAL. Intel also faces more competition from outside the traditional IBM-style PC market, which it has long dominated. IBM's and Motorola Inc.'s PowerPC chip, used in Apple Computer Inc.'s Power Macintoshes, threatens to become a strong rival. And emerging markets for cable-TV set-top boxes and video-game machines—which mostly use other chips—could draw consumer dollars away from PCs.

That's why Intel, which still owns over 75% of the \$11 billion microprocessor market, plans to spend a record \$2.9 billion on new plants and equipment, up 20% from 1994. That dwarfs AMD's planned \$700 million. Those new plants will have plenty of chips to churn out. This spring, Intel is expected to introduce new, faster Pentiums. And they're 30% cheaper to produce, thanks to a more advanced manufacturing process. That will allow Intel to keep cutting prices while maintaining high profit margins.

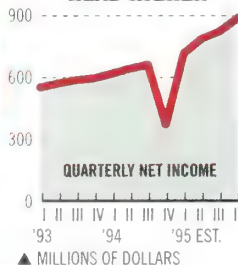
Intel's next big weapon: the P6. With 6 million transistors—twice as many as Pentium—it's likely to be big and expensive at first, so it won't sell in quantity until 1996. But by borrowing speed-enhancing tricks from rival chips such as the PowerPC, the P6 runs nearly twice as fast as the swiftest Pentium. That will keep PC makers in the Intel camp, says Linley Gwennap, a consultant and editor of the industry newsletter *Microprocessor Report*.

Even though rivals gradually are gaining on its microprocessor technology, the Pentium is keeping Intel firmly in the lead. By the end of December, 42% of PCs sold at retail

INTEL'S PENTIUM TAKES OFF...



...AND PROFITS HEAD HIGHER



re Pentium machines, says market researcher ARS Inc. in Irving, Tex. (chart). "Our sales are through the roof," says Mark Wahrman, director of merchandising for J&R Computer World, a New York City retailer. Now, with the prime consumer-PC buying season over, Intel will have to persuade corporate buyers to upgrade to Pentium.

So far, they've held off because of

the higher prices. Indeed, some observers, such as Compaq, think Intel is trying to move PC buyers to Pentium too fast. After all, the 486 still has legs: It will continue to outsell Pentium in 1995. AMD's triple-speed version of the 486 actually outperforms low-end Pentiums for most applications, at a much lower price. Says AMD Chairman W.J. "Jerry" Sanders III: "Intel is trying to push

the market before the market is ready."

Ready or not, though, the market still is willing to let Intel call the shots. Says Robertson, Stephens & Co. analyst Daniel L. Klesken: "Even through all this brouhaha, the Pentium has missed barely a heartbeat." With bugs and lawsuits put to rest, it's Intel that's likely to give rivals palpitations from now on.

By Robert D. Hof in San Francisco

ADVERTISING

NUNS ON THE NET, SOFTWARE IN THE SOUK

Computer makers are reaching beyond geekdom with MTV-style ads

late January, and William H. Gates III is in Las Vegas for the Consumer Electronics Show. In the midst of meetings in his hotel room, a football game plays in the background. An ad for IBM comes on—a new one, featuring French men discussing computers as they stroll along the Seine. Suddenly, Microsoft's chief executive is enthralled. "What's this?" he demands, jacking up the volume to hear the French dialogue, loosely translated on the screen in

an analyst at Wasserstein Perella & Co.: "Across the board, you see a change in the way that computer companies want to be perceived by the public."

The new look for advertising by IBM, DEC, and Microsoft is no accident: All three have hired new agencies to revamp their images. Last August, DEC awarded its account to DDB Needham Worldwide, dropping several agencies including Ciociola & Co. and Ketchum Advertising. Microsoft last June hired

on a new way of using lasers to store 10 times more data. "Cool," the first man replies. Another commercial in the series features a group of nuns walking in a Prague convent, with one complaining that her PC needs a new operating system. In a dig at Microsoft, she says she is waiting for Chicago, but that Microsoft's new operating system keeps getting delayed. A fellow nun tells her that she was just reading about the new OS/2 Warp from IBM in *Wired* magazine. Realizing this might give her access to the Internet, the nun's face lights up, and she replies: "I'm dying to surf the net." A third scenario takes place in a Moroccan souk.

PAPER CUT. Microsoft's new ads also have an international flair. One intersperses images of various software programs with flashes of people from different cultures. In another, a boss throws

ADBANGER

Digital's ads mix rock music, flashing lights, and racing images while superimposing statements to the company's prowess



SISTER ACT

One IBM spot, replete with goofy subtitles, has a gaggle of Czech nuns singing OS/2 Warp's praises as a gateway to the Internet

English subtitles. "It looks pretty cool." Comment ça? The boy wonder of the software biz finding something—anything—cool about IBM? Don't be shocked. Blue's latest commercials really are pretty hip. And with computer companies increasingly targeting sales to the home, it isn't the only one with a raft of trendy new ads aimed at a mass audience. Digital Equipment Corp. launched new MTV-like commercials on Thanksgiving, and Microsoft is pouring \$100 million into an offbeat TV campaign of its own.

BUMMER, NON? Not all computer companies are aping the strategy. Apple Computer Inc.'s new 30-minute infomercial and Compaq Computer Corp.'s current campaign focus on how computers can solve real-life situations without any added ambience. But, says Karen R. Ficker,

Wieden & Kennedy, the Portland (Ore.) firm that created Nike's "Just Do It!" campaign. The IBM ads are the start of a new worldwide campaign by Ogilvy & Mather Worldwide Inc., which pulled off a major coup last year when it wrested the \$400 million-to-\$500 million IBM account away from some 40 other agencies. Says Matthew Ross, the Ogilvy & Mather senior vice-president who handles the IBM account: "We want to demonstrate to people that IBM is more approachable and human than they thought."

What are the ads like? In the commercial that Gates saw, the French-speaking senior citizen gripes to his friend that his hard drive is "maxed out"; the friend finds that a "bummer" but reassures him that IBM is working

a business report down a spiral staircase. Message: Software beats paper.

DEC's ads, which have the look and beat of music videos, may represent the biggest departure from traditional computer advertising. The spots are set to original rock music, and bright flashing lights complement racing images. One flashes several images of mass destruction such as fires and floods and in big block letters: "HELL HAS OUR PHONE NUMBER." This format is repeated in a number of versions of the commercials, which aired from Thanksgiving to New Year's and will reappear in February.

Cool, for sure. The big question now: Does cool sell computers?

By Lori Bongiorno in New York, with Richard Brandt in Las Vegas and bureau reports

DISASTERS

THE HOPE BENEATH THE RUBBLE IN JAPAN

Ironically, the quake may give the economy a long-term lift

One of the oldest aphorisms in Japan is *jishin, kaminari, kaji, oyaji*, or "earthquakes, thunder, fire, and father"—the things Japanese fear most. That's why, since watching the devastation of last year's earthquake in Los Angeles, Japanese authorities assured citizens that local construction codes would prevent freeways from tumbling and buildings from toppling.

So much for official assurances. Measuring 7.2 on the Richter scale, the quake that hit Japan just before dawn on Jan. 17 was 10 times stronger than L. A.'s, tearing apart expressways and buildings. Its death toll is likely to top the 3,769 dead and missing in Japan's last major quake, in 1948. Kobe, with 1.5 million residents, was hit hardest.

Now, a shocked Japan faces a repair bill estimated at \$60 billion—and Standard & Poor's Corp. warns that hidden structural damage could dramatically boost the tab. Meanwhile, the quake may have ripple effects overseas—on companies ranging from insurers to notebook computer makers.

Still, in cold economic terms, the devastation looks manageable. Commerce in the affected areas of Hyogo and Osaka, which account for 12.2% of Japan's gross national product and 16% of retail and wholesale sales, will slow. Even though such companies as Matsushita Electric Industrial Co. say profits may be hurt, reconstruction spending could boost Japan's economy by 1.5% over two years, says J.P. Morgan & Co. economist Jesper Koll.

STATESIDE HELP. New investment in public works nationwide could provide further economic stimulus. Although Japan's quake codes are tougher than those in the U.S., "we have to rethink some of our guidelines and strengthen existing roads, train tracks, and old buildings," says Keiichi Otani of the National Research Institute for Earth Science & Disaster Prevention in Tsukuba.

Can Japan's strapped financial system cope? Markets, at least, are voting yes. The Nikkei stock average dropped just 0.6% in the two days following the jolt. One reason: Japan's Finance Ministry already is considering low-interest reconstruction loans to small com-

panies funded by the nation's \$1.9 trillion Postal Savings System. And the Bank of Japan is ready to extend cheap loans to insurers to encourage rapid claims payouts. In the end, S&P figures even Japanese insurers may not have to take much of a hit, because what quake insurance there is in Japan is largely reinsured overseas. Says Robert J. Mebus, managing director of S&P's Insurance Rating Services: "We think we'll find bits and pieces [of



Japan has tougher codes than the West, but it also suffers worse jolts. The pressure is on to reinforce existing roads and buildings—and erect sturdier new ones

KOBE: THOUSANDS DEAD, BILLIONS IN DAMAGE

problems] among insurers in the U.S."

Still, many Japanese businesses will suffer. Industries from steel to electronics to beer are already coping with severe damage. At Kirin Brewery Co.'s Kansai facility, for example, the earthquake took out 1.5 million liters of bottled beer worth \$8 million and halted production. Some observers are fretting about higher steel prices in Asia since many furnaces are built around Kobe.

Japan's vaunted just-in-time inventory system and export machine also

will be fouled up by twisted rails and crumpled highways left by the quake. "The major concern I have is the transportation infrastructure," says Ed Brogan, an analyst at Jardine Fleming Securities Ltd. in Tokyo. Indeed, road damage has cut off exports by Omron Corp., a Kyoto components maker, even though its plants were untouched.

RIPPLE EFFECT? The effects on computer makers could ripple worldwide. Some 20% of the world's liquid-crystal-display production—used mainly in notebook computers—is concentrated in Hyogo and Osaka. Display Technologies Inc., a joint venture between IBM and Toshiba Corp., will lose several days of production at its Kobe area plant, where it makes high-grade thin-film transistor screens. And LCD maker Hosiden Corp. has a plant in the heart of Kobe and a new facility under construction. Even

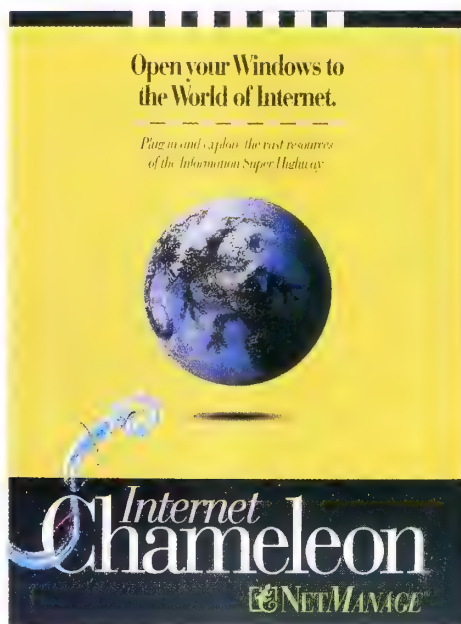
if such plants aren't badly damaged, logistical problems could temporarily halt shipments of LCDs.

Japan already is girding for the Big One many experts think could hit Tokyo one day. Design codes and safety measures probably will get stricter. "Our thinking has been too lax," says Otani. In a nation perhaps more alert to the dangers of earthquakes than any other, that's a telling admission.

*By Robert Neff and
Larry Holyoke in Tokyo*

THE INTERNET

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EDITED BY KEITH H. HAMMONDS

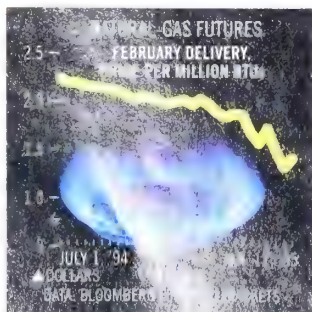
ATTENTION, K MART PRESIDENT

JOSEPH ANTONINI'S DAYS AT Kmart may be numbered. The retailer's board on Jan. 17 stripped Antonini of his chairman's post, naming outside director Donald Perkins to the job. Although Antonini retains the titles of president and CEO, his credibility is waning, say outsiders. "The handwriting is on the wall," says a headhunter. How could he keep his job? Produce quick gains in the retailer's sagging profits. "There has not yet been a turnaround engineered," says Jim Severance, portfolio manager for Wisconsin's state investment

CLOSING BELL

OUT OF GAS

Go ahead: Crank up the heat. Natural-gas prices have virtually collapsed, with February futures down 24% since the start of the year. Why? Look out the window. Utilities and other big gas buyers stocked up for an ugly winter like last year's, encouraged by strong domestic production and abundant Canadian imports. So far, they've seen only balmy conditions, which have cut into demand. That has made for "a worst-case scenario" for prices, says Smith Barney analyst John Saucer. Still, prices firmed on Jan. 16 and 17 with predictions of colder days ahead.



board and organizer of a shareholder revolt last June. Severance hopes for improvements by June.

ORANGE COUNTY: GEE, WE HAD NO IDEA

DERIVATIVES? LIKE, DUH. FOR managers who once had \$20 billion to invest, the folks running Orange County are trying hard to appear financial innocents. In testimony before a special state senate panel, a parade of county executives said they were unaware of the risks that led to the county's bankruptcy filing and losses of nearly \$2 billion. "I had never owned a share of stock," testified former Treasurer Robert Citron, who said he relied on investment houses such as Merrill Lynch. Citron's deputy, Matthew Raabe, said he didn't grasp "the somewhat bizarre aspects" of the high-risk investments that sank the fund. Merrill said it "did not create or direct the county's investment strategy."

SAATCHI & SAATCHI SAYS NO & NO

SAATCHI & SAATCHI ISN'T EXACTLY in the mood to forgive and forget. The advertising giant on Jan. 16 rejected an offer for ousted chairman Maurice Saatchi to return to the fold. The overture was made through S.G. Warburg by Maurice's older brother Charles, with the understanding that the original ad network named after the brothers would one day be spun off to them. Saatchi's Bates Worldwide would remain in the group. A company spokesman says the offer was dismissed out of hand. The company is suing its ex-chairman for poaching staff, stealing files, and soliciting clients. Maurice is countersuing for breach of contract and is setting up a rival agency.

HEADLINER

TYSON'S TIME TO FLY THE COOP

Insider trading charges. Cattle futures. Mike Espy. It hasn't been the sort of send-off that Don Tyson might have expected after 50 years in the chicken business. Besides the investigations into his company's controversial ties to the Clinton Administration, Tyson Foods under Tyson last year lost a hostile bid to take over a turkey producer. It also had to take the first major write-off in its history.

No matter: On Jan. 13, Tyson announced he would step down as the company's chairman come Apr. 21. The decision, he says, "had

nothing whatsoever" to do with questions about his relationship with the Clintons. Tyson says he is leaving because he wants to honor a little-known contract he signed a decade ago that called for him to retire on his 65th birthday.

"I started with this company at 14. I've put in 50 years, and now it's time to move on," says Tyson, whose father founded the poultry giant as a one-truck business in 1935. He will be succeeded by Leland Tollett. But Tyson still will head the board's executive finance committee.

By Stephanie Anderson Forest



IS FIRST FIDELITY FIXING FOR A SALE?

FIRST FIDELITY BANCORP IS prettying itself up. The bank announced on Jan. 18 that it is laying off 1,000 employees and shutting down several dozen branches. The Newark (N.J.) bank may be simply cutting costs, following the lead of many others in the industry. Or it may be slimming down for an eventual sale. A source at the bank says NationsBank took a look at First Fidelity's books last summer; two other major banks have since done the same. None of the banks would comment.

A NINTENDO NOOSE FOR SAMSUNG

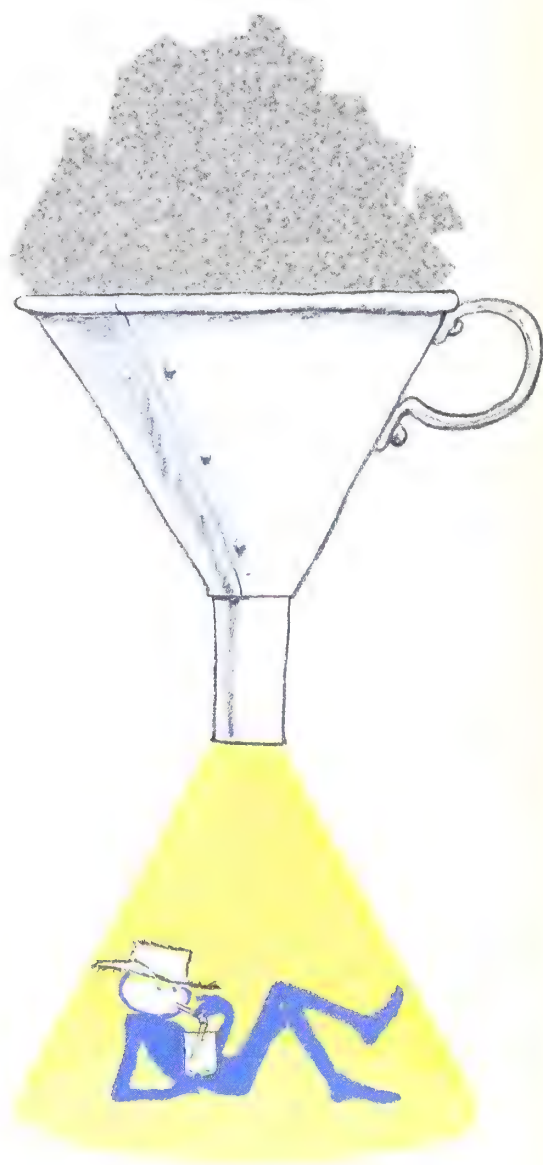
POW! CRASH! LAWSUIT! AFTER repeatedly warning Korean giant Samsung to stop making memory chips encoded

with counterfeit video-game programs, Nintendo of America says it discovered Samsung's name under a layer of black epoxy in a pirated copy of the megahit Donkey Kong Country. On Jan. 18, Nintendo filed a multimillion-dollar suit against Samsung, which also makes memory chips for legitimate Nintendo video games. Nintendo says it has not decided whether to cut off Samsung as a chip supplier. Samsung denies knowing of any counterfeit activity.

ET CETERA...

- Borland International will cut 650 jobs, a week after CEO Phillippe Kahn left.
- David Edelstein has to excuse himself from overseeing IBM's consent decree.
- Some 6,600 auto workers struck General Motors' big parts plant in Flint, Mich.
- Dan Dorfman on Coca-Cola: May buy Quaker. Coke on Dorfman: Clueless.

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our chemical waste into **energy**?



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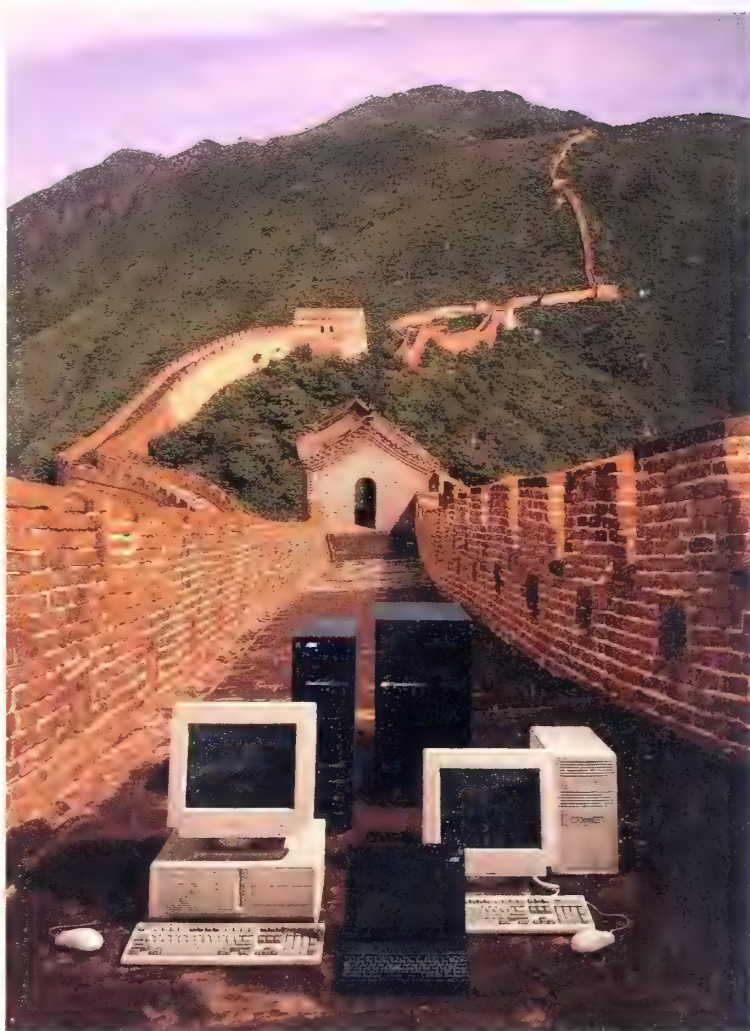
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CLINTON COULD WIND UP LOOKING LIKE THE HEAVY ON IMMIGRATION

Determined to move right on social policy in the wake of the Republican rout, the Administration is rapidly earning a reputation as the Gang That Couldn't Pander Right. Case in point: White House plans to get in sync with the GOP's anti-immigrant thrust by weighing new restrictions on legal aliens.

Politically, the idea seemed like a winner inside President Clinton's rapid-response White House. California voters had overwhelmingly backed a ballot measure denying social services to illegals. Clinton's approval ratings in the Golden State are in the tank. And Republicans were vowing to slash welfare costs by throwing legal immigrants out of public assistance. What could win more votes with angry nativists than a tough immigration policy?

But Clintonites hadn't counted on GOP leaders growing queasy over the immigrant-bashing coming from the party's order-state governors—now that the election is behind them. The bizarre reversal: National Republicans are softening their stance just as Clinton may knuckle under.

House Speaker Newt Gingrich signaled a shift on Jan. 9 when he said the GOP might ditch plans to deny legal immigrants welfare payments. Gingrich wasn't—as is his custom—just musing out loud. Other leading Republicans, among them Jack Kemp and New York Governor Christine Todd Whitman, warn that the assault could alienate minorities. The GOP won 30% of the Hispanic vote on Nov. 8, and party pros want to expand that base. Despite his broad powers, Gingrich doesn't speak for the entire GOP. Representative Lamar S. Smith (R-Tex.), chairman of the House immigration subcommittee, sees a "crisis situation" in welfare costs: "Legal immigrants tend to take advantage of the generosity of the American taxpayer."

With such America First sentiment percolating through the

electorate, the White House wants to appear tough. The results will be seen in a Clinton immigration-reform plan due in February. "Neither side wants to be outposted on this," says Stephen Moore, an economist at the libertarian Cato Institute.

The big news in the White House effort is that it may include curbs on legal immigration as well. That approach has powerful backers on Capitol Hill. Both Smith and Senator Alan K. Simpson (R-Wyo.), head of the Senate immigration panel, favor such limits: Simpson introduced a bill in the last Congress to cut legal immigrants from 675,000 to 500,000 per year for five years. While Clinton hasn't yet signed off on a measure, options before him include eliminating slots for employees brought in by businesses and reducing quotas for countries with relatively few visa applicants.

BIG BROTHER. House Majority Leader Richard K. Armey (R-Tex.) and Senate Judiciary Committee Chairman Orrin G. Hatch (R-Utah), both pro-immigration libertarians, will likely join Gingrich in pressuring Smith and Simpson to back off on legal entrants. GOP leaders also look askance at proposals to set up a national verification system to help employers sniff out illegals. While the Administration is

likely to endorse measures that would create a monitoring system—such as upgrading immigration and Social Security databases—Gingrich & Co. may shy away from a proposal many right-wingers see as endorsing a Big Brother ID card.

Where does this leave the White House? Potentially, looking politically crass just as the GOP looks responsible. "The dumbest thing the White House could do," says immigration lobbyist Rick Swartz, "is let Gingrich and Armey win the hearts of the ethnic community by being more pro-immigrant than Clinton." But that's exactly what could happen in the strange world of Washington immigration policy.

By Catherine Yang



ELLIS ISLAND: Fewer tired and poor?

CAPITAL WRAPUP

BALANCING ACT

Although a balanced-budget amendment to the Constitution is likely to pass Congress soon, states may be reluctant to ratify it. A new study shows why: A balanced federal ledger could cost the states \$67 billion a year in aid from Washington, estimates Steven D. Gold at the nonpartisan Center for the Study of the States in Albany, N.Y. Worse, says Gold, the GOP's \$200 billion tax-cut plan could cost states billions in revenues since more than 40 tie their tax codes to the federal system.

FIRST... SORT OF

► The good news for Bill Clinton is that he leads Democrats in the latest New Hampshire Presidential poll—if you don't count "undecided." The bad news: He was chosen by just 24% of 600 Granite State Democrats surveyed by American Research Group on Dec. 19-29. Clinton beat ex-Governor Mario Cuomo (21%), '92 rival Paul Tsongas (11%), retired General Colin Powell (10%), Vice-President Al Gore (5%), and civil rights activist Jesse Jackson (2%). The undecided vote was 27%.

RETREAT ON REGS

► Comptroller of the Currency Eugene A. Ludwig is poised to retreat from a contentious plan to make lenders report race and gender breakdowns for small-business and farm loans. The new Community Reinvestment Act reg, proposed last fall, sparked protests from the industry and the Federal Reserve. But with the shift to the right in Congress, regulators say the reporting rules will likely be cut back or dropped when new CRA regulations are issued this year.

EUROPE

THE FINANCE VIGILANTES ARE CLOSING IN

As the markets punish Europe's weaklings, hopes for monetary union fade



adapt to and thrive in an open global economy, and those whose balance sheets classify them with the emerging markets.

Already, investors are demanding fat risk premiums from countries whose policies continue to foster inflationary spending. Long-term money in Italy or Spain costs almost 500 basis points more than it does in Germany—nearing the 600-point spread between Mexican government bonds and U.S. Treasuries.

CHOKES OFF. The gap between European haves and have-nots is likely to get even wider soon. With Germany's economic recovery further along than its neighbors', most analysts believe the Bundesbank will raise interest rates by midyear to keep inflation at bay. That will put pressure on the other EU nations to keep up. But raising rates in countries that are only now emerging from recession could choke off growth prematurely—and pump up the deficits of Spain, Italy, and Belgium even further.

Italy may be the most dramatic example of a country pushed to the brink by market turmoil. A crisis of political confidence drove the lira to a historic low against the German mark before the naming of an emergency technocrat government on Jan. 16 calmed the markets down. Now, Acting Prime Minister Lamberto Dini is in a race

Depending on whom you talked to, the European aftermath of Mexico's peso crisis was either a triumph or a disaster. At their monthly meeting in Brussels on Jan. 16, Europe's finance ministers congratulated themselves on how well their currency markets had weathered the storm. French Economy Minister Edmond Alphandéry even said optimistically that the European Union could achieve monetary unity on schedule by 1997.

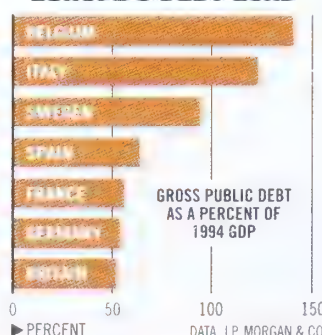
Meanwhile, in London, Swiss Bank Corp.'s head of global foreign exchange thought just the opposite. After watching the financial markets hammer Spain, Italy, and Sweden—calming down only when the U.S. announced it would bail out Mexico—Andy Siciliano saw worse to come for the EU. "Bringing together Europe's disparate economies will never happen," he said.

Indeed, the recent bond and currency turmoil seems to prove that the financial vigilantes are closing in on Eu-

rope's economic weaklings. Traders are piling into the mark and fleeing weaker currencies—in effect, voting against high levels of public debt and stagnant fiscal policies in Europe's more profligate nations. Says Peter Praet, chief economist at Générale de Banque in Brussels: "What the market is telling European governments, and what is not being understood, is that it wants the welfare state reformed."

As investors continue to favor the most solvent and reform-minded countries, the threads that hold together the EU's crowning achievement—its single market—could begin to unravel. Over time, chronic currency and bond weakness could even split Europe into two ranks of countries: those that

EUROPE'S DEBT LOAD



...t time to overhaul Italy's costly pension scheme and rein in the 1995 budget deficit. Although trade unions and the business community applaud his agenda, former Prime Minister Silvio Berlusconi could make it tough for Dini to push debt-busting measures through Parliament before another election is called.

Other European governments, from London to Helsinki, are scrambling to improve their budget numbers before creditors punish them further. In early January, Sweden unveiled a four-year budget program intended to cut \$15 billion, or 7% of gross domestic product, from annual state outlays to stabilize the debt. In Spain, the scandal-racked government of Prime Minister Felipe González on Jan. 13 approved a cost-tightening budget package intended to cut \$1.1 billion in spending.

HITTING TAXPAYERS. But such steps fall short of the spending cuts the markets are demanding. Bo Engstrom, Stockholm analyst for James Capel & Co., thinks that Swedish bonds and the krona will get pummeled again as the minority government tries to push the package through Parliament. And while the Madrid-based España Managing Director Alain Dreyer calls the Spanish government's stance "important," he worries that it won't change the overall environment, which he characterizes as "a lack of confidence" in governments around southern Europe.

If governments try hitting taxpayers to finance their spending, they could derail the consumer phase of recovery that has so far been an export-led recovery. And slower growth could get dangerous. Lehman Brothers Inc. analyst Keld Holm estimates that if the U.S. GDP growth averages 2% per year for the remainder of this decade, its budget deficit will actually be 10% higher in 2000 than it is today. As a result, he says, "it won't take a recession but only the signs of a slowdown" for markets to push up the risk premium for each of Europe in what he predicts could be a "nightmare scenario" of low revenues, higher debt, and rising interest rates in some of the weaker members.

At that point, European governments will have no choice but to reach for a half-finished remedy—inflating their currencies—to reduce their debt burden. That might kill once and for all the idea of a broad monetary union in Europe. Between the two versions of stability offered by Europe's politicians and the global capital markets, there's no doubt where the odds lie.

*By Bill Javetski in Paris, with
via Sonsoni in Rome and bureau
reports*

MEXICO

WASHINGTON TO THE RESCUE. NOW, ABOUT THE PRICE...

Furious wheeling and dealing over terms of a Mexican bailout

Senate Foreign Relations Committee Chairman Jesse Helms (R-N.C.) wants Mexico to make illegal immigration a criminal offense before the U.S. shells out a dime of emergency aid. House Democratic Whip David E. Bonior of Michigan insists that Mexico boost wages and U.S. imports. And Patrick J. Buchanan wants the Mexican government to put the state oil company, Pemex, on the auction block.

All that sound and fury emanating from Washington has been sparked by the Clinton Administration's proposed \$40 billion in loan guarantees to rescue the Mexican economy. Yet despite the vocal protests, a deal is falling into place—because the U.S. capital's premier power brokers have joined forces to see to that.

Even so, nailing down details of the plan is proving tough: Congress is demanding ironclad assurances that Mexico will pay stiff risk premiums and embark on stringent economic reforms before any U.S. taxpayer money is exposed. And lawmakers want the terms of the deal made explicit. But the Mexican negotiators, sensitive to domestic resentment of U.S. dominance, want to keep their concessions out of the public glare.

NEW WAVE. However the two sides handle the diplomatic cover, key elements of the package are emerging. The Mexicans will have to pay a fee of around 10% of guaranteed loans they draw on. By contrast, Israel paid a 4.5% premium for U.S. guarantees on loans to build housing for refugees from the former Soviet Union. The Mexicans also will have to pledge oil revenues as collateral. And U.S. officials expect Mexico to make deep cuts in government spending and sell off state-owned industries. "We don't want this to be a bargain for the Mexicans," says a U.S. official.

Although the conditions may be hard

for the Mexicans to swallow, too much is at stake for either side to walk away from the financial crisis touched off by the sharp devaluation of the peso. Without a quick infusion of aid, Mexico's crisis would only worsen. For the Americans, that raises the prospect of a new wave of illegal immigration. Moreover, Mexico's economic failure would be a major strain on the North American Free Trade Agreement.

SCARY SCENARIO. That's why U.S. officials, including Treasury Secretary Robert E. Rubin and Federal Reserve Chairman Alan Greenspan, scrambled to put together the package. They quickly won support for the bailout plan from both House Speaker Newt Gingrich (R-Ga.) and Senate Majority Leader Bob Dole (R-Kan.).

The stiff terms will add to Mexican President Ernesto Zedillo Ponce de León's political woes. Already unpopular, Zedillo is eager to avoid charges that he is turning Mexico into a U.S. colony. But neither can Mexicans afford to quibble over appearances. Mexico's banking system is reeling from the devaluation and is likely to suffer further losses from the resulting economic slowdown. "Without an influx of dollars, the banking system is going to decompose," says Lawrence D. Krohn, chief Latin American strat-

egist for Union Bank of Switzerland.

Visions of that scary scenario are what drove Mexican officials recently to press Washington for more aid above a previously announced, U.S.-led \$18 billion international credit line that failed to calm the markets. No matter what the final terms of the deal, one thing already is clear: Mexico has reverted to its traditional role as a financial ward of the U.S.

*By Amy Borrus and Dean Foust in
Washington, with Geri Smith in Mexico
City*



PAINFUL CHOICES

Zedillo is eager to avoid charges he's turning Mexico into a colony

INDIA

INDIA SHAKES OFF ITS SHACKLES

Free-market reforms are stirring up the country's long-stagnant economy



NEW DELHI DISH:
Deregulation is giving the telecom industry a boost

vestment is expected to rise sharply.

At a time when Western investors are skittish about emerging markets, India still looks attractive. Unlike Mexico or China, it has a full-throated democracy that should make it more stable as it faces the challenges of reform. And unlike Asian countries with overheated economies, India's growth has been more moderate. "India is just now on the upside of its cycle, while every East Asian country is at the top or beyond," says Jim Rohwer, chief economist for Asia at CS First Boston.

Old portraits of Marx, Lenin, and Stalin are common on the streets in India's lush southern state of Kerala, once a Communist Party stronghold. Yet as India moves away from decades of socialist planning toward more market-oriented capitalism, the pictures are fading from neglect—and Kerala's business scene is brightening. "Industries are popping up all over the place," says M. C. Mycle, branch manager of Citibank in the Kerala city of Ernakulam, as he sips tea with local businessmen in his office. "Money is really flowing in."

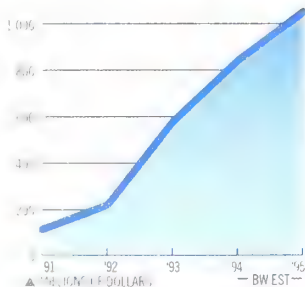
For locals alike, the busi-

ness climate in India is looking up. After nearly four years of market reforms, Prime Minister P.V. Narasimha Rao's policies are starting to pay off: Industrial output is rising at an 8% annual clip, economic growth is likely to hit 7% this year, and foreign in-

India could even begin to gain ground against rival China. While dozens of major power projects in China have recently been stalled by Beijing bureaucrats, India is about to close deals worth \$5 billion for eight privately financed power plants. "A year ago, U.S. companies were all over China," says U.S. Assistant Energy Secretary Susan F. Tierney, who has made several trips to India to advise New Delhi on its new power plants. "Now the momentum has shifted to India."

That was clear during Commerce Secretary Ronald H. Brown's mid-January trip. Chief executives from 25 companies accompanied

FOREIGN DIRECT INVESTMENT IS RISING



THE LATEST DEALS

COMPANY/PRODUCT	VALUE (MILLIONS)
ENRON Offshore oil and gas	\$1,100
MISSION ENERGY Power	\$400
SOROS FUND Petrochemicals	\$200
DAIMLER BENZ Autos*	\$160
DAEWOO Autos*	\$100
U S WEST Telecoms	\$100

*Joint venture

DATA: BUSINESS WEEK

own to three Indian cities. Contracts for tentative deals worth more than \$4 billion were announced. Among the biggest projects, California's Mission Energy Co. signed an agreement with Tata Group, one of India's largest industrial concerns, for a \$400 million power plant. U.S. West Inc. announced a \$100 million investment to provide a pilot project in India's first privately operated telecommunications service.

Overall, nearly one-third of the \$7 billion in direct foreign investment approved since 1991 has been from U.S.-based multinationals such as General Electric, Wrigley, and Kellogg. Companies such as Ford Motor Co. and American International Group Inc., which haven't yet cracked the market of 900 million people, are banging on the doors.

Not surprisingly, India is starting to loom larger for U.S. policymakers after decades of icy relations. A few weeks before Brown's trip, Defense Secretary William J. Perry was in New Delhi to sign a historic military-cooperation pact, including joint training and collaboration on weapons production.

The U.S. attention is coming even though Rao is facing one of the worst political fights of his tenure. In local elections in December, populist policies of reforms dealt a stunning defeat to his party in state elections. Rao may fall from power if his party fares no better in state elections coming up in February and March. With that in mind, Rao's government is likely to pull back on a handful of the reforms that are most threatening to farmers and workers (table).

But confidence is high among many Indian executives that the fundamentals of Rao's free-market push will remain intact—no matter who is in power. "The reforms have become institutionalized," maintains Urjit R. Patel, the International Monetary Fund's India representative.

IPS AND CHOCOLATE. Evidence of the government's new, open attitude can be seen throughout the country. Delivery trucks loaded with once banned foreign products such as Ruffles potato chips and Nestlé Crunch bars rumble over the whole highways across the subcontinent. Advertisements for AT&T's "communications solutions" are plastered on New Delhi streets, signs of upcoming liberalization in the telecom industry. And some 280 foreign institutions have

crowded into India's financial industry, which had been closed to outsiders before 1992.

To be sure, there are limits on how far foreign investors can go. Bureaucrats are still reluctant to allow foreigners 100% equity. Some projects approved in New Delhi bog down at the state level, "where you still have to go through the same old socialist rigmarole," says Subramaniam Swamy, chairman of India's Commission on Labor Standards & International Trade.

Nevertheless, the contrast with the old days is stark. Prior to 1991, getting a project through the bureaucracy "was

economic takeoff remains its backward infrastructure. The country has just 9 million phone lines—one for every 100 people—and has one of the world's lowest per-capita consumption rates of electricity. The government is responding by opening its telecom and power sectors to private investors. On Jan. 16, India invited bids for franchises to offer cellular and basic telephone services. Already, AT&T, U.S. West, and British Telecommunications have each formed ventures with local partners. In the deal announced during Brown's trip, U.S. West said it would install a phone system serving 40,000 customers.

In power, India needs to raise some \$200 billion to meet its goal of adding 142,000 megawatts of capacity over the next 15 years. Financing has already been lined up for the first three plants, all involving U.S. companies. The projects include a \$920 million plant by Enron Inc.

MOMENTUM. As it attempts to catch up with East Asia, India's challenge is to balance its reforms against the tremendous needs of India's impoverished millions. Most analysts agree that while Rao's government has done a good job selling its policies to foreign investors and India's business elite, it has failed to explain what's in it for farmers, workers, and the poor. To head off unrest, the new budget to be unveiled in mid-February by Finance Minister Manmohan Singh is expected to boost subsidies for agriculture, increase pension payments, and provide more aid to the unemployed. The budget deficit is likely to grow from around 4.5% of gross domestic product to more than 6%.

With \$20 billion in foreign exchange reserves, vs. \$1 billion in 1991, India can afford a little social spending. And few in India believe there will be much backsliding if Rao's party loses power. Even his top foes don't talk about bringing back the License Raj. The opposition Bharatiya Janata Party, for instance, distrusts foreign consumer-goods companies such as Coca-Cola Co. but has long advocated a greater role for the private sector. That's why even though there may be fits and starts, the momentum of India's reforms will continue to push the world's second-largest country into the global economy.

By Sharon Moshavi and Pete Engardio in New Delhi, with Shekhar Hatangadi in Bombay, Dave Lindorff in Hong Kong, and bureau reports

ALTHOUGH SOME REFORMS WILL STAY ON HOLD...

- Reforming labor laws that make it extremely difficult to lay off workers
- Privatizing money-losing state-owned enterprises in transportation and financial services
- Eliminating subsidies for commodities such as rice, wheat, and corn
- Allowing 100% foreign ownership of companies in consumer goods, telecoms, and autos

...THE HEART OF THE PROGRAM IS ON TRACK



POLITICAL TIGHTROPE:
Prime Minister P.V.
Narasimha Rao

- Opening power and telecommunications projects to foreigners
- Speeding approval of manufacturing investments by foreign and domestic investors
- Reducing import barriers on everything from garments to computers
- Allowing private sector to compete with national monopolies in railroads and postal services

like peeling an onion," recalls Suresh C. Rajpal, president of Hewlett-Packard India Ltd. "With every layer you peeled, your eyes watered." Now, clearing components through customs takes two days instead of three weeks. Under the old system, derisively dubbed the License Raj, Indian companies waited months for government approval of routine business such as expanding production or hiring a director. Diversifying into a new product could take years. Now, family-dominated empires such as the Tata, Birla, and Godrej groups are restructuring, finding foreign partners, and devising export strategies.

One of the biggest obstacles to India's

EDITED BY STANLEY REED

TOOTH AND CLAW IN MOSCOW: THE REFORMERS BITE BACK

After weeks of chaotic signals from the Kremlin, an authoritative-looking Prime Minister Viktor Chernomyrdin finally appeared on television on Jan. 16. He announced new efforts to end the bloody debacle in Chechnya and pledged that economic reform would stay on track.

There was an almost audible sigh of relief in the foreign investment community in Moscow. Chernomyrdin, who is respected by foreign investors and international aid officials, has been nearly invisible in recent weeks as hard-liners, including Security Council boss Oleg Lobov and Alexander Kozhakov, head of the presidential bodyguard, vastly increased their clout. These men are believed to have pushed President Boris Yeltsin into the messy Chechen war. And they've leaked xenophobic charges that Western aid programs, including financier George Soros' efforts to aid Russian science, are really fronts for espionage.

Among these officials, the most outspoken on economic matters is Vladimir Polevanov, the new privatization chief. He wants foreigners banned from buying into "strategic" industries, such as aluminum, energy, and defense. Meanwhile, he has banished foreign advisers from his offices, even though some played key roles in creating the highly successful sell-off program.

SERIOUS DAMAGE. But in the past few days, Chernomyrdin and his deputy, former privatization boss Anatoli B. Chubais, have counterattacked, stripping away some of Polevanov's authority. Now they're trying to reassure Western governments and investors.

Whatever the outcome, serious damage has already been done. Foreign investment has slowed to about \$50 million a month, or 10% of August's volume. Without the Chechnya debacle, Chubais believes, it could have reached \$3 billion per month by spring. "Whatever money was going to come in will be less," says Bernard Sucher, a Moscow-based broker. In ad-

dition, \$15 billion in aid from the International Monetary Fund is in jeopardy.

The uncertainty will continue, because the power struggle isn't over between the reformers and those who want to turn back the clock. The former—the Chernomyrdin group—have close ties to officials in energy companies, such as Gazprom and Lukoil, who stand to get rich from stock shares if privatization and foreign investment flourish.

They are opposed by the defense and intelligence chiefs and Deputy Prime Minister Oleg N. Soskovets, who is backed by the managers of largely obsolete smelters, steel mills, and weapons factories. Unlike the energy companies, these industries will be big losers if privatization proceeds. They aren't likely to get much foreign investment, and they face huge layoffs as state subsidies dry up.

SCARING PEOPLE. Moscow analysts believe that the hard-liners engineered the Chechen conflict as a prelude to bringing back some state economic control and media censorship—and perhaps even staging a coup. But so far, they haven't accomplished much more than scaring people.

Even so, the feud is hurting foreign investors. While reformers did manage to eliminate oil-export quotas, the Kremlin chaos also brought new restrictions on foreign oil companies' access to pipelines that threaten such projects as Conoco's \$385 million Polar Lights venture.

All this is embarrassing to President Clinton, whose devotion to the increasingly erratic Yeltsin is already under fire from the new Republican majority in Congress. The Administration's hope is that the Chechen war can be ended and reformers can regroup and win back their influence. But that's far from a sure thing: The hard-liners have made their strongest stab at control yet, while Yeltsin is looking like a spent force.

*By Peter Galuszka in Moscow,
with Amy Borrus in Washington*



CHERNOMYRDIN: *Taking the lead*

GLOBAL WRAPUP

HUNGARY ANNOYS INVESTORS

► Hungarian Prime Minister Gyula Horn, by wrecking the privatization of a chain of state-owned hotels this month, has shown that Central Europe's ex-communist rulers could be a big drag on the march to market economies. They tend to juggle the interests of their old-line supporters with the need to attract investment, producing erratic policy.

In the hotel deal, Horn fired the respected privatization commissioner Ferenc Bartha and raised the price—

even though American General Hospitality, a Dallas hotel-management company, had already won a tender at \$57.5 million. "In making concessions to the left, he shot himself in the foot," says one investment banker. "It sends a very bad signal to investors."

Horn may now try to redeem himself by speeding up state sell-offs and appointing a credible successor to Bartha. Meanwhile in Poland, Prime Minister Waldemar Pawlak, another ex-communist, dithered for months before signing off on the privatization of some 400 companies late last year.

MINORITIES IN BRITAIN

► Minority hiring, never much of an issue in Britain, may come under more scrutiny. A survey released Jan. 18 by the government's Commission for Racial Equality concludes most big companies do little to assure equal opportunity in employment beyond verbal support for the idea. Many said they have no policy to spur minority hiring and no plans to create one. British law bans race bias but sets no affirmative-action criteria. The minority jobless rate is more than twice that for whites.

GOD, FAMILY, AND DOMINO'S -THAT'S IT'

Tom Monaghan has sworn off the costly distractions that nearly cooked the pizza chain



SOLD THE LUXURIES: A once flamboyant Monaghan runs a stripped-down chain

Even during the wild 1980s, the heyday of executive ostentation, pizza baron Thomas S. Monaghan stood out. The founder of Domino's Pizza didn't just indulge his three passions—God, Frank Lloyd Wright, and racing things—he did so with a singular and of gaudiness and eccentricity. For a headquarters, he spent \$150 million on a half-mile-long copper-and-steel tribute to the Wright Prairie style in Ann Arbor, Mich. Plans called for a story tower cantilevered 15 degrees to the east—a leaning tower of pizza—that was never built. On surrounding land, he installed a petting zoo and loose herds of cows and buffalo. Instead, there were a \$40 million collection of Wright artifacts and drawings, a mime theater directed by Marcel Marceau, and a two-story personal office suite with vaulted ceilings and leather tiles on the floor. Monaghan bought everything from the Detroit

Tigers to an island in Lake Huron. A Word of God Catholic, he decried abortion and built a cathedral in Nicaragua.

Then, he disappeared from sight. Since 1992, Monaghan has avoided the limelight while Domino's veered into deep financial trouble and back. As his banks pressured him to sell his playthings at fire-sale prices, rivals Pizza Hut Worldwide and Little Caesar Enterprises Inc. gained valuable ground. Domino's has finally recovered, but only after write-offs totaling \$117 million. In 1994, the company says its earnings hit \$30 million while revenues, including franchise sales, inched up 5%, to \$2.5 billion (charts).

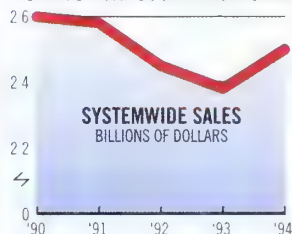
ADIEU, PERKS. What happened is a classic case of a CEO intoxicated by his own success. And Monaghan knows it. Never one for meek gestures, the pizza baron is as zealous in his penitence as he was in his spending. His office now is a small, windowless closet of a room situated just

off the two-story suite. He flies coach and hasn't had a bodyguard in years. He insists he doesn't read newspapers or watch TV—too distracting. He has even given up his prized architectural journals. "I don't even look at 'em," he says. "I decided those things aren't important. God, family, and Domino's—that's it."

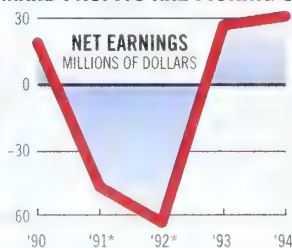
The company's 1,200 franchisees are just happy Monaghan has relaxed his management style. Many say that the company's biggest problem during the crisis was the chairman's autocratic insistence that Domino's stick to its 32-year formula of hawking only pizza and Coke, while rivals sold an array of popular items like breadsticks and salads. At the prodding of a former Little Caesar's executive who lasted at Domino's just 20 months, Monaghan has allowed the first new products in decades. Hits like thin-crust pizza and buffalo wings have fueled the sales rebound. "What we needed,"

Domino's Fights Back

SALES ARE CLIMBING AGAIN...



...AND PROFITS ARE PICKING UP



*INCLUDES WRITE-OFFS OF \$67 MILLION IN 1991 AND \$50 MILLION IN 1992

DATA: DOMINO'S PIZZA INC.

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BusinessWeek **ONLINE**

Whether Domino's is out of the woods isn't clear. The pizza market is in the doldrums, as low-priced hamburgers steal more fast-food dollars

s franchisee Glenn Mueller, "was a willingness to listen to customers."

Despite his excesses, Monaghan comes across as likeable and forthright, almost naive. Sitting in his tiny office, sipping from a bottle of water, he gladly explains how he ran into so much trouble. The buying that so tantalized him, he says, was a direct result of "going without" as a child. After growing up in a Catholic orphanage and foster homes in Michigan, "I liked luxuries and was willing to work for them," he says. "Everything I bought, I thought I could justify: It was good PR [for Domino's]." The one thing he couldn't justify in terms of business was a \$3 million home designed by famed architect Faye Jones. It was to anchor another Monaghan project: a housing development in Ann Arbor featuring a Robert Jones golf course and a requirement that all homes be built by one of

30 top architects chosen by Monaghan. "It would be the architectural showcase of the world," Monaghan says. But "with a Catholic upbringing, you're not supposed to enjoy things that much."

In late 1989, Monaghan happened to read a book called *Mere Christianity* by C.S. Lewis. Chapter 8, on pride, floored him. "It was a rude awakening," he says, "I realized pride was the biggest of all sins." He halted the house and swore off the buying binge. He left day-to-day operations at Domino's and put the company up for sale.

CRIPPLING FEES. Trouble was, Monaghan's finances were so commingled that potential buyers couldn't figure out what they were buying. The Wright-inspired headquarters was also an albatross. It was so expensive to build, says one Michigan real estate expert, that rents couldn't cover the mortgage. Even now, says Chief Financial Officer Harry

Silverman, Domino's loses money on it.

After 2½ years and no sale, Monaghan decided to retake the helm. Sales were slipping, and money-losing assets were crimping cash flow. Executives were preoccupied by the incessant talk of a sale and were hog-tied by Monaghan's absentee decision-making. Pizza Hut, meanwhile, had begun a huge assault on the delivery market, and Little Caesar's was snagging business with clever marketing and budget pies.

By 1992, Monaghan fell into technical default on nearly \$200 million in debt. Domino's was generating cash, but declining sales alarmed a global web of 30 bankers. Because personal and corporate debt were cross-collateralized, one default caused, well, a domino effect. Asset sales cut costs, but bank fees from ongoing technical default were crippling.

"There was lots of liquidation, and it happened very fast," says one Ann Arbor real estate investor. Monaghan sold the Tigers to Little Caesar's founder Michael Ilitch for about \$85 million. That was \$32 million more than he paid in 1983, but failed to cover his total investment in the team. He also lost money unloading more than 100 expensive autos. An \$8 million Bugatti Royale cleared only \$5

REENGINEERING MANAGEMENT

THE MANDATE FOR NEW LEADERSHIP

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JAMES CHAMPY

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million. He had invested \$28 million in Drummond Island, the Lake Huron resort, but sold it for \$3 million. It was a bloodbath.

Monaghan did better restructuring the company. He computerized the stores to improve flow of market information. And he separated the accounting for company-owned stores from franchises so he could see how profitable they were. "You find out you weren't making as much money as you thought," Monaghan says. So, he closed or sold to franchisees 1,000 company stores and axed 600 administrative jobs.

The main chore, however, was restructuring the debt. Twice, in 1992 and 1993, Domino's failed with bond offerings. The first time, Salomon Brothers Inc. couldn't find enough buyers. The second flopped when Domino's lost a \$78 million judgment in St. Louis after one of its drivers allegedly ran over a woman in his rush to deliver a pizza. That forced Domino's to give up its trademark 30-minute delivery guarantee.

Finally, after the new-product push generated a full year of better results, Domino's was able to put together a new bank syndicate last May. The new financing featured just eight primary banks and a 20% drop in interest expense, according to CFO Silverman.

IN LIMBO. Whether Domino's is out of the woods isn't clear. The new-product boost is good news. So is the fact that in 1994, Little Caesar's sales were flat, while Merrill Lynch analyst Allan Kaplan estimates Pizza Hut profits declined 18%. Unfortunately, value pricing in the hamburger business is clobbering pizza as a whole. And Domino's sales are under pressure from a franchisee cooperative that is selling cheese, dough, and other ingredients to Domino's stores in competition with the parent company. Commissary sales make up a full 40% of the parent's revenues of \$850 million.

For the time being, Domino's will ride on its recent success. But fast-food consumers are fickle, and Monaghan's company has never been adept at product development. Larry Sheehan, the ex-Little Caesar's executive who fathered the new-product push, is long gone after a bitter pay dispute with Monaghan. His replacement, fast-food veteran Anthony M. Lavelly, has yet to earn his stripes in pizza.

John H. Schnatter, founder of pizza purveyor Papa John's International Inc., insists that "Domino's is in a reactive state." Monaghan, however, is as sanguine as ever. "We were in limbo," he says. "Now the word I use—and it doesn't excite anybody—is 'focus.'" A little focus goes a long way. Domino's has had enough excitement.

The Corporation

STRATEGIES

RON LaBOW'S STEELY RESOLVE

Poison pill or no, the WHX chief won't give up on Teledyne

Investment banker Ronald LaBow is not one to walk away from a challenge. In the late 1980s, the little-known financier battled Goldman, Sachs & Co. and Oppenheimer & Co. for control of bankrupt Wheeling-Pittsburgh Steel Corp. LaBow became chairman when the company emerged from Chapter 11 in 1991—and it's now one of the most profitable steel-makers around.

So when news came early in January that the board at conglomerate Teledyne Inc. had adopted a poison pill to defend against a takeover by WHX Corp., Wheeling-Pitt's recently formed holding company, LaBow was undaunted. An avid mountain climber—one whose tenacity in negotiations and eye for hidden value have made him one of Wall Street's leading "vulture" investors—LaBow clearly is not going away.

GOBBLING UP. Far from it: On Jan. 13, WHX got antitrust clearance to raise its 1.8% stake in Teledyne to 15%—and on the following Tuesday, volume in Teledyne shares soared. WHX won't confirm it's buying. But sources close to LaBow, 59, say he's intent on gobbling up the \$2.49 billion conglomerate. His advisers say he's considering launching a proxy fight. LaBow's target is Teledyne's overfunded \$1.9 billion pension plan: Huge layoffs left it with \$860 million in surplus assets. Teledyne's \$634 million specialty-metals business could be another juicy morsel.

So far, Teledyne's board refuses to negotiate with WHX, in part because it

doesn't believe LaBow is playing straight. In November, LaBow tried to talk to Teledyne founder Henry E. Singleton. Together with allies, Singleton controls 22% of Teledyne's stock, and he sits on the board. Leon Cooperman, a former Goldman Sachs partner and a Singleton confidant, says LaBow asked him to set up a meeting with Singleton.

LaBOW'S TURNAROUND AT WHEELING-PITTSBURGH

1987-91 After beating Goldman Sachs in a fight for steelmaker Wheeling-Pitt, investment banker Ron LaBow is named chairman when W-P emerges from Chapter 11 in 1991. LaBow and partners control 55% of W-P shares.

1991-93 LaBow cuts workforce by 7%, slashes expenses, and spends \$69 million modernizing plants. As steel demand improves, operating earnings soar from \$13 million in 1991 to an estimated \$84 million in 1994.

1993-94 LaBow raises \$400 million in three equity offerings, cuts debt from \$350 million to \$270 million, and builds a war chest of \$440 million. Also diversifies, buying downstream steel users to boost margins.

LATE 1994 LaBow sets his sights on Teledyne for its \$860 million in surplus pension assets and specialty-metals operations. Teledyne rejected LaBow's \$1.2 billion bid: He's now studying a proxy fight.

Cooperman claims LaBow assured him he would go away if the talks went nowhere. But after Singleton passed word to LaBow to send a proposal to the board—and Teledyne rejected LaBow's \$1.2 billion bid—LaBow turned hostile. "He assured me this would be friendly and quiet," says Cooperman. "This is not a man to be trusted." LaBow declined BUSINESS WEEK's request

**HOT ROLLS
W-P WANTS
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COILED ST**

an interview. Teledyne hit back with poison pill letting stockholders buy shares at a 50% discount if anyone buys more than 15% without board approval. LaBow's lowball bid also rankled. Although the \$22-a-share bid was 28% above Teledyne's November share price, analysts say Teledyne's value is closer to \$30 a share. Last July, investment bank Donaldson, Lufkin & Jenrette Inc.—was hired to advise LaBow—estimated that an acquirer would retain roughly \$1 billion of Teledyne's pension surplus. So LaBow is bidding just \$700 million for the rest of the company.

WHAMASH. Teledyne's rejection leaves LaBow contemplating the chances of success in a proxy fight. "Our mission now is to change the board's mind," says a source close to LaBow. "Or change the board." LaBow is counting heavily on shareholder discontent. The company's whamash of unrelated businesses—and its stock price—have performed poorly in recent years. Under strong shareholder pressure, CEO William P. Rutledge has

WHX has reason to covet Teledyne. Wheeling-Pitt could use the surplus pension assets to offer its own workers a richer retirement package—in exchange for concessions in upcoming negotiations with the United Steelworkers. Analysts say Wheeling-Pitt also wants to cut its workforce. The easiest route: an early-retirement package for aging workers, funded by Teledyne.

Sources close to WHX say Teledyne's specialty-metals businesses also fit into LaBow's plans. Since 1993, LaBow has diversified away from commodity hot-rolled steel products with a series of acquisitions and joint ventures with niche producers and high-margin downstream steel users. Adding Teledyne's specialty-metals unit, with products such as tungsten and titanium, would help. "It would solve LaBow's strategic objectives of upgrading his product mix," says Aldo J. Mazzaferro Jr., steel analyst at C.J. Lawrence & Co. LaBow would likely sell Teledyne's aviation, electronics, and consumer-products units.



Teledyne,
a loose
consortium
of lackluster
businesses,
may be rife
with unhappy
shareholders.
Its biggest
lure: a
pension plan
overfunded by
\$860 million

ent two years streamlining and says Teledyne "is about to see improved results." LaBow's advisers claim they've seen "a huge indication" that shareholders want the company sold. Gerald B. Warner, whose money-management firm, Warner Rosenthal McGwynn Inc., holds 10% of Teledyne's stock, agrees. "It has a lot of businesses that would be better owned by other people," he says.

Wall Street has so far shown little confidence that LaBow will succeed. Investors fear he underestimates the complexity of dislodging the closely regulated pension funds. "It comes down to: 'Whose money is this?'" says Jon Kutler, head of Los Angeles' Quarterdeck Investments. "It's not all Teledyne's, and the government isn't going to stand by and let an outsider get at it."

LaBow is no stranger to financial maneuvering. A bankruptcy specialist at New York investment bank Neuberger & Berman, he left in 1989 to form a partnership that bought up the secured bank debt of bankrupt Wheeling-Pitt. With an estimated investment of \$140 million—much of it borrowed—he gained control. "LaBow can spot an undervalued asset," says one former Neuberger associate. "He's usually several steps ahead of most people." But if he's a top-flight financier and negotiator, the intensely private LaBow has won few friends. "He can be intimidating. He makes people feel like they're in a courtroom," says D. Leonard Wise, a former Wheeling-Pitt CEO and now chairman of North Carolina Steel. "He's not a people person."

BULGING WAR CHEST. After Wheeling-Pitt emerged from Chapter 11, LaBow promoted its chief operating officer, James L. Wareham, to chief executive. Wareham negotiated more flexible work rules and spent \$69 million modernizing Wheeling-Pitt's plants. That cut costs sharply, just as steel prices rose. Now, operating profits per ton, at \$39, are the third-highest in the industry. Analyst Mazzaferro says operating income has risen sixfold since 1991, to an estimated \$84 million in 1994, on sales of \$1.13 billion, an 18% increase.

Such performance has allowed LaBow to raise \$400 million in three stock offerings since 1993 and to cut debt 23%, to \$270 million. With cash flow soaring—to \$140 million in 1994, up from \$18 million two years earlier—LaBow has built up a \$440 million war chest for acquisitions. Along the way, he also cashed in. By 1992, LaBow held 45% of Wheeling-Pitt. Now he holds 15%—worth \$57 million—and he's made an estimated \$56 million through equity sales.

There are still doubts about LaBow's strategy. WHX has also bought five radio stations—and a dog-racing track in West Virginia. Questions over where LaBow is headed—along with the prospect of a lengthy proxy fight—have unnerved WHX stockholders: Shares now trade around 14, well below their 1994 high of 21. "I don't think the Teledyne deal helped," says G. Kenneth Heebner, portfolio manager at Capital Growth Management, which holds 1.7 million shares. "People don't understand his plans."

A successful bid for Teledyne would mean sharply higher debt—and if LaBow can't sell off Teledyne's lackluster assets quickly, WHX may fall back onto the corporate sick list. As LaBow contemplates the climb up Mt. Teledyne, it's not clear that his shareholders will go along.

By Keith L. Alexander in Pittsburgh and Eric Schine in Los Angeles



Cover Story

KODAK'S NEW FOCUS

An inside look at George Fisher's strategy

Not long after taking the helm of Eastman Kodak Co. in late 1993, George M.C. Fisher bought a new house. Not just any house. He and his wife, Ann, chose a spacious estate on East Avenue, a boulevard that strikes out from the center of Rochester, N.Y., and meanders into the suburbs. On the very same road, a few miles closer to town, sits another house once owned by a Kodak chairman named George: the 50-room mansion built in 1905 by George Eastman, the company's visionary founder. Coincidence? Fisher thinks it could be more like destiny.

Acutely aware that the responsibility for restoring Eastman's legacy rests on his shoulders, Fisher has mentioned their common address on more than one occasion. He often jokingly refers to Eastman as "the other George." And he likes to point out parallels between his strategy and the game plan of Kodak's founder, who combined technological genius with something of a short supply at the company recently—marketing vision.

Not many executives would compare themselves to one of the icons of American industry. But George Fisher, 54, doesn't lack self-confidence. In giving up his CEO post at fast-growing

Fisher's Bold Beginning...

RED STRATEGY Company had been floundering, unsure which businesses to pursue. Fisher decided that photography was key to the future and sold Kodak's health and household-products arms.

RED DIGITAL IMAGING UNIT With product development and sales scattered among divisions, digital imaging was ill-focused. Fisher gathered most of the unit into one division and hired an experienced computer marketing executive to head it.

RED BALANCE SHEET By selling off businesses, notably the Sterling drug operation, he has slashed the company's total debt from \$7.5 billion to \$1.5 billion. Photography cash machine is now available to fund growth, not debt payments.

RED MORALE After years of restructurings and uncertain direction, employees were disheartened. By painting a bright future and improving communication, Fisher has perked up spirits.

RED OVERHAULING CULTURE By stressing accountability, and cycle time, Fisher is beginning to reform Kodak's slow-moving culture. Made pay is now dependent on performance.

And The Challenges Ahead

RED RATE GROWTH Fisher believes Kodak can double its growth rate in photography, a tough challenge in the growing global market. Key target: Asia, especially China, where Kodak lags behind Fuji.

RED NEW TALENT Company needs outside blood. So Fisher has hired a new CFO and head of digital marketing. Badly needs marketing depth.

RED FOCUS ON CUSTOMER Kodak still is driven by engineering mentality that devises products first and then finding buyers. Company must become more market-savvy.

RED JOINT VENTURES Kodak can't do it alone in digital imaging. Company has to expand its technology base. Its platinum rolodex should work here. Promise of joint announcements in 1995.

RED COSTS FURTHER Plenty of fat still around. Big targets include receivables, inventories, corporate overhead. No way Kodak can compete in digital arena with its high cost structure.

When George Fisher came to Kodak, he traded a virtually sure thing for one of America's toughest management challenges. Kodak had spent billions on research and development, diversification, and repeated restructurings. Fisher's immediate predecessor, Kay R. Whitmore, implemented no fewer than five reorganizations—yet Kodak earned less in 1993 than it had in 1982. Although blessed with a powerhouse brand name, it seemed trapped in the slow-growth photography industry, hobbled by huge debts, a dysfunctional management culture, and a dispirited workforce.

It's too early to say whether Fisher can yet lay claim to the other George's crown. But after barely a year at the helm, Kodak's new chief has clearly shaken up the sluggish giant as never before. He has sold off its health-care businesses and refocused the company around its core imaging business. Asset sales have also allowed him to slash the photography giant's debt load from a burdensome \$7.5 billion in 1993 to an estimated \$1.5 billion last year.

Far less tangible but no less crucial to Kodak's future has been Fisher's progress in reinvigorating a bloated, hierarchical management system, which deflected responsibility for poor performance. And although morale is still shaky, Fisher has given staffers hope that the company has a future beyond repeated restructurings. "I'd call George's first year a spectacular success," says University of Michigan management professor C. K. Prahalad, who has consulted for both Kodak and Motorola. "He has cleaned up the company and created a new spirit, a new willingness to compete. He has laid the foundation."

Now, Fisher has to deliver. His strategy, as outlined in several lengthy interviews with *BUSINESS WEEK*, is fairly straightforward. First, he'll continue to work on Kodak's culture and costs. "There are textbook types of things that are wrong with this company," he says. "Decisions are too slow. People don't take risks." So Fisher is applying lessons learned at Motorola: By focusing on basics such as quality, customer needs, and shorter product-development time, he hopes to squeeze out costs and produce a more dynamic culture. He says results should start to show this year, but he believes it'll take three to five years to see dramatic progress.

The go-slow approach stands in sharp contrast to the rapid-fire job cuts and reorganizations practiced by many other CEOs who parachute into troubled companies. But Fisher thinks cost-cutting edicts from on high don't work well. He prefers to set tough goals, then let his managers decide how to achieve them. Moreover, Fisher fears drastic action could kill Kodak's golden goose: its consumer photography operation, which produces 75% of its operating profit on just 42% of its revenue. "There's no need to take a business with the share and profitability we have and screw it up by replacing experienced managers and injecting outsiders," he says.

That leads to his second goal: reignite growth. Fisher is convinced that Kodak's traditional film and paper business can grow at 7% to 9% annually for the next decade, about double the growth rate in recent years. How? In part, through expansion in the fast-moving economies of Asia, where Kodak has been badly lagging archrival Fuji Photo Film Co. And he sees dramatic growth in barely tapped developing markets such as Russia, India, and Brazil. "Half the people in the world have yet to take their first picture," says Fisher. "The opportunity is huge, and it's nothing fancy. We just have to sell yellow boxes of film."

"STEP-BY-STEP." Fisher is also counting on strong growth from Kodak's thus-far disjointed entry into the digital imaging market. Kodak's boss has gathered the company's far-flung digital projects into a single division and hired Carl Gustin, a former Apple Computer Inc. and Digital Equipment Corp. marketing executive, to head the unit. By embracing digital technology, he hopes to enhance photography—and encourage more picture-taking. "The future is not some harebrained scheme of the digital Information Highway or something," he says. "It's a step-by-step progression of enhancing photography using digital technology."

The new emphasis on digital technology is already producing results. Early in 1995, Kodak will relaunch its poorly marketed Photo CD product to make it more useful to millions of desktop personal computer users (table). Another promising product: the new CopyPrint station, which uses digital technology to make enlargements from ordinary prints

Cover Story



MAKING PHOTO CDs

Fisher has unified the company's disjointed efforts in digital technology.

(page 68). None is exactly revolutionary. But again, the model is Motorola, which succeeded by pushing low-cost electronics items that turned into hits. "I'd bet we have at least one home run of the sort Motorola hit in cellular telephones," says Fisher.

It's a tantalizing turnaround plan. But so far, critics complain, progress is slow. Few on Wall Street expect good news on Jan. 31 when Kodak announces its 1994 results. The company has already hinted at more restructuring charges. Analyst B. Alex Henderson of Prudential Securities Inc. estimates that Kodak's earnings from continuing operations fell 4% last year, to \$953 million, as its revenues rose by 7%, to \$13.7 billion. At around 48, Kodak stock is little changed since Fisher's arrival in December, 1993.

TOUGHER THAN MOTO. Even some Fisher boosters caution that he has taken on a monumental task. The core photography business is brutal, marked by growing capacity and falling prices. Just to keep profits flat, Kodak needs to cut manufacturing costs substantially every year. "This is a tougher challenge than Motorola," says Richard S. Braddock, former chairman of Medco Containment Services Inc. and a Kodak outside director. "Kodak has very high shares and high margins. That's a difficult combination. While trying to be aggressive, you're also trying to defend what you have."

In the digital imaging arena, Kodak has a very different problem: It's just one of many hopefuls in a nascent industry. By its own count, Kodak faces no fewer than 599 global competitors working on optical storage technology that could challenge its Photo CD. And other rivals are chasing after the emerging digital market. Casio, for example, just introduced a \$700, feature-laden digital camera. In other niches, ranging from scanners to printers, Kodak faces such giants as Canon,

Fujitsu, Sony, and Hewlett-Packard. "Kodak has some good technology," says Jacques P. Kauffmann, an imaging consultant in Wilmette, Ill. "But they haven't yet shown any outstanding products. So far, they're just one player among many."

And fixing a deeply ingrained culture in a company with 88,000 employees could prove harder than Fisher realizes. Lower-level staffers complain that the changes haven't filtered down to them; decision-making is still painstakingly slow, and they remain confused about Kodak's direction. Many skeptics would agree with the assessment of a longtime institutional investor in Kodak. "Fisher is a great manager in a tough environment," he says. "In a situation like

that, very often the environment wins."

Still, even the naysayers aren't about to count Fisher out. Few CEOs boast his credentials as a technologist and manager. After getting his PhD in applied mathematics from Brown University, he started as a scientist at Bell Labs. In 1976, he moved into management at Motorola, where he quickly made his mark as head of the pager division by breaking into the Japanese market. In 1988, Fisher took on the CEO's title.

As Motorola's CEO, Fisher excelled at motivating people, pushing decision-making down and picking among the company's many promising technologies. Profits more than doubled during his tenure. But when the Kodak search committee came calling, Fisher was ready to listen. "I was already

Kodak's New-Product Offensive

ADVANCED PHOTOGRAPHIC SYSTEM "Smart" film and camera be introduced in 1996. Stores data, such as shutter speed, on film as each picture is taken, permitting much finer processing and printing.

IMPROVED SINGLE-USE CAMERA

To be introduced in the U.S. this spring. Sleek plastic design and better flash mark

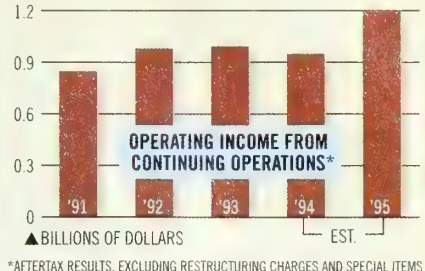
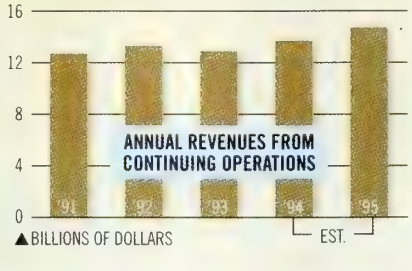
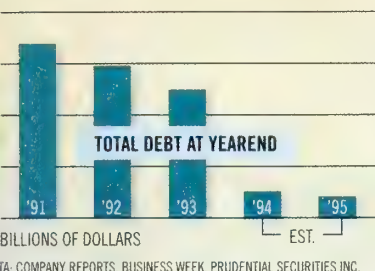
big improvement over

old disposable cameras.



PHOTO CD Relaunch planned March. Kodak will seek to revive product by marketing it to desktop-computer users.

KODAK'S DEBT LOAD IS DOWN... ...THOUGH SALES GROWTH IS SLOW... ...AND PROFITS ARE UNEVEN



success," he recalls. "But I was too young to begin to think about the end of my career. This was a chance to take a great company, like Kodak, that was having some transient problems, and build it back up into one of the world's great companies." A \$2 million salary, \$5 million signing bonus, and some juicy stock options helped seal the deal. Once he arrived, it didn't take Fisher long to focus on Kodak's most visible problem: its balance sheet, weighed down by nearly \$7.5 billion in debt. Much of that was the result of acquisitions, notably Sterling Drug Inc. in 1988. A lot of cash being generated by photography was going to service debt instead of funding new products and businesses. "We're going to milk the imaging business to death," says Fisher. By February, 1994, he decided on a dramatic measure: sell the sprawling health and household-products divisions. **STODIAL MENTALITY.** The resulting auctions brought in \$1 billion. By yearend, Kodak's debt was down to \$1.5 billion, cutting annual interest payments by 80%, to \$120 million, freeing up much of the company's cash flow to back Fisher's new strategy. Just as important, the massive sale transformed Kodak from a conglomerate to a narrowly focused imaging company, making it easier to manage. Kodak executives say the quick decision to sell the non-imaging operations was vintage Fisher. He rarely handles a stack of paper twice and usually gives executives a decision on the spot. That's a dramatic change at a company where analysis by analysis had become an art. "People can study a problem around here forever," says Leo J. Thomas, the executive vice-president who heads the imaging group. "George has a willingness to use the 80/20 rule," which holds that it's better to be right just 80% of the time if you act quickly. The push for quick decision-making is part of a broad cam-

paign by Fisher to overhaul Kodak's lethargic culture. When Fisher arrived, he found an insular company that venerated authority and frowned on confrontation. "It was so hierarchically oriented that everybody looked to the guy above him for what needed to be done," he says. That led to diffusion of responsibility: "How can you hold a person accountable if you've had three overrides on his decision?" he asks. Having been beaten down so long, he says, Kodak developed a custodial mentality geared to protecting current businesses rather than seeking new frontiers. "Why is Kodak in such a state of doldrums and Motorola so vibrant?" he asks. "One drives for growth, and the other doesn't. You have a different mental attitude when you drive for growth. You don't just try to figure out how to manage your way through existing markets."

To help break down the rigid hierarchy and get his message across to all layers of the company, Fisher has turned himself into an ambassador of informality. Low-key, genial, he almost never raises his voice or shows anger. Past Kodak CEOs tended to be aloof and autocratic. But managers liken Fisher's style to that of a coach—or a parent. "It's like talking to your father," says Carl F. Kohrt, general manager of the \$1.6 billion health sciences unit. "You don't want to disappoint him."

Fisher is also far more accessible and visible than previous Kodak CEOs. He frequently pops in on researchers for updates on projects and chats casually with staffers in the cafeteria, where he breakfasts almost every workday—invariably on a bowl of Special K cereal and a mug of coffee. Employees are invited to send him E-mail messages, and they do—as many as 30 a day. His secretary prints them out, and he usually responds the next day with handwritten notes on the printouts—a personal touch staffers seem to appreciate.

More important, Fisher is trying to teach his managers that Kodak's ultimate fate rests on them. During management presentations, Fisher often flashes a slide with a single word on it: accountability. Kodak managers have frequently missed targets by a mile and suffered no consequences—but no longer, Fisher vows. In the annual planning process for this year, he worked hard with executives on coming up with realistic numbers and has been adamant that he will hold laggards responsible. And in late January, he plans to announce a new management-compensation structure that will tie pay more closely to performance. Kodak won't discuss details.

Kodak executives concede that many employees are reeling from the shift in direction. Staffers are also angered over

“People’s feelings about the company are still on a roller coaster”

PRINTERS Kodak's \$10,000 thermal printer is a leader, producing near-photographic-quality prints. Company aims to get \$1,000 version to market in 1996.

PRINT STATION Allows consumers to make high-quality prints and enlargements from ordinary prints, not negative. Combines a scanner, PC, and thermal printer.

DIAPHRAGM CAMERA Introduced in mid-1995. Has Apple's name on it, but makes it. First low-cost (\$700) digital camera for consumer applications.

OLD FILM Replacement for high-end Ektar film is well-received.



Cover Story



◀ ON THE I-WAY

Few corporate chieftains can boast Fisher's credentials as a technologist



▶ 'A NEW SPIRIT'

Fisher's quick decisions and a sense of accountability are still novel at Kodak

a Fisher-ordered cutback in benefits last summer. And an announcement in December that 800 more jobs would be cut at the Kodak Park manufacturing complex in Rochester has further soured the air. "People's feelings about the company are still on a roller coaster," says Kohrt.

But Kodak execs say there's progress. In the labs, Kodak never used to measure the time it took to complete projects or even how fast they were progressing. With Fisher's emphasis on cycle time, managers have set up formal gauges.

The labs are key because the new, improved Kodak will need things to sell. Fisher has been spending a disproportionate amount of time on a subject dear to his technologist's heart: digital imaging. The term has been around since the late 1970s, when Kodak executives first realized that chemical-based photography faced a new rival. Images could be captured with digital cameras, stored on computer disks, altered with software, and zapped around by phone wires.

Kodak began frantically spending huge sums on digital-imaging R&D—as much as \$5 billion over the past decade. But by the time Fisher arrived, little had emerged from the labs. Some executives were gung ho, others fearful of introducing digital gear that would cannibalize high-margin film and paper sales. To compound the problem, product development and sales efforts were scattered over more than a dozen divisions.



▲ APPROACHABLE

Fisher has turned himself into an ambassador of informality

At one point, Kodak was working on 23 separate digital scanner projects.

Fisher ended the debate. Kodak would push full-speed into digital imaging: "And if that eats up some of the film business, so be it." He also folded most digital efforts into a new Digital & Applied Imaging Div. To run it, he turned to Gustin, one of sev-

eral outsiders Fisher hired to help him revitalize Kodak's management. An ebullient former advertising executive who talks at a rapid clip, Gustin says he was amazed at the technology languishing in Kodak's closet. Outsiders agree that Kodak has top technology in several key digital imaging areas. Among them: color-management software to ensure true reproduction and charged-couple devices (CCDs) that act as the eyes for digital cameras and scanners. One big problem, Gustin quickly surmised, was lack of marketing ability. To help overcome that drawback, Gustin is on the verge of hiring a half-dozen experienced computer marketing executives. Fisher has also hired former Apple Chairman John Sculley as a part-time marketing consultant in the digital-imaging area.

Thanks to the reorganization, Gustin claims he and his team will soon silence critics who believe stodgy Kodak is incapable of achieving the six-month development cycles typical in the computer industry. Back in November, Gustin says, he started a project to develop a \$1,000 desktop version of a

Outsiders say Kodak has world-class technology. The problem has been a lack of marketing ability

17-month-old, \$10,000 color thermal printer that spits out high-quality color images on special paper using a heat-transfer process. That version weighs about 60 pounds and has 500 parts. In less than a month, he says, Kodak engineers built a 4-pound, 65-part prototype with better performance specs. Gustin promises a raft of new digital products early next year. In addition to the less expensive thermal printer, he's aiming to introduce a \$300 digital scanner and a digital camera in the \$300 range. Apple's QuickTake digital camera, made by Kodak, is among the cheapest now on the market, at \$700. Gustin's division had revenues of about \$500 million in 1994, roughly 4% of Kodak's total sales. Gustin has told Fisher that sales will grow by 67% in 1995 and will take another leap the following year. Meanwhile, Gustin is looking to resurrect Kodak's faltering Photo CD project. Launched in mid-1992, it was widely misdirected at the consumer market as a high-tech way to see photos on TV. But few photo buffs wanted to spend out \$1 to transfer each snapshot to a compact disk. In March, Kodak will relaunch Photo CD, this time aimed at the PC market. By adding software to each Photo CD platter, Kodak aims to make it easier to retrieve photos and use them in electronic documents. A personnel manager, for example, could load a Photo CD with pictures of employees into a CD-ROM drive and attach an organizational chart complete with photos.

Although digital imaging embraces everything from Sega video games to on-demand cable-TV movies, Kodak is sticking mostly to its historical niche of color still images. That's plenty big enough market, says Gustin, who says Kodak wants to make it cheap and easy for people to use high-quality images in everything from real estate listing sheets to school essays. But Kodak hasn't have the clout or the technology to do it alone. That's why Fisher and Gustin have been trying to get other industry players to adopt Kodak's technologies as standards in the computer and multimedia worlds. Fisher's Continuum Rolodex of information-industry contacts has been crucial in the hunt. He used his contacts at the University of Illinois' National Center for Supercomputing Applications in a drive to get Photo CD accepted as a standard for sending images over the Internet. He has also met with other corporate heavyweights—among them Microsoft's Bill Gates and Matt McNealy of Sun Microsystems—to discuss licensing and partnership deals. Microsoft will include Kodak's color management standards in its Windows 95 operating system. Kodak also says it's working with leading telecommunications companies on ways to make it easier to send images over phone lines. And on Jan.

17, Kodak said it would license a technology from Live Picture Inc. that will speed image processing on Photo CDs. Other deals should be announced in the first quarter.

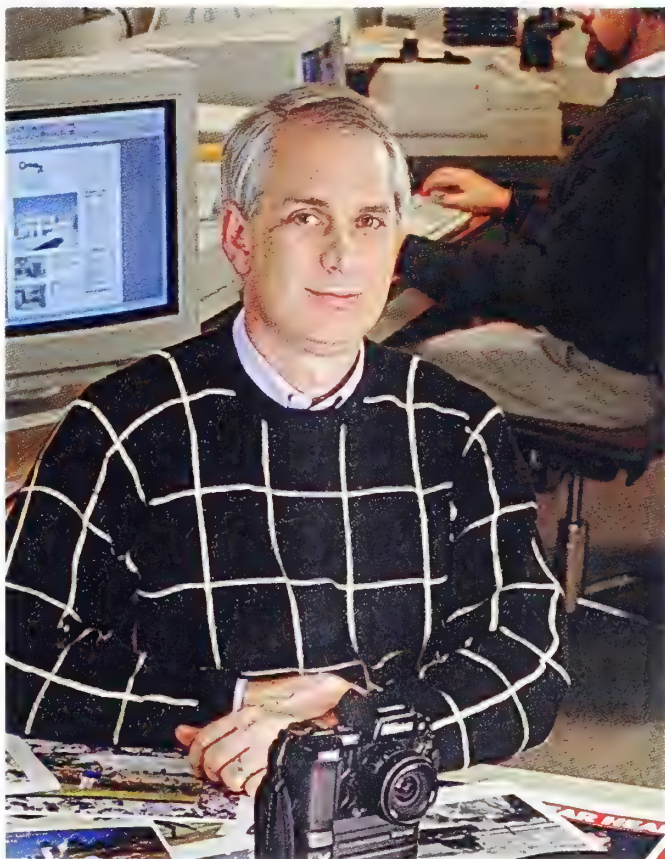
Again, while the strategy sounds fascinating, skeptics abound. Bob Goldstein, president of ZYZX Visual Systems, a Los Angeles imaging lab, is one of the leading Photo CD users in the country. But he has been frustrated because key enhancements, such as the ability to encrypt images, have been repeatedly promised by Kodak but never delivered. "I'm going to reserve judgment until I see the products actually hitting the street," he says.

TRANSFORMATION. Others point out that Kodak has never been good at manufacturing electronic gear in high volumes and low cost. Nearly all of its equipment is aimed at the less competitive, pricey end of the market, from copiers to scanners. And when Kodak tried to sell consumer products in the past—8mm camcorders, videotape, even batteries—it quickly dropped out when the competition got too stiff. "They're going into a totally different business, with totally different distribution channels and much slimmer margins," says one former Kodak executive. "They have an incredibly long road ahead."

Fisher concedes Kodak is still feeling its way in the digital world. His aim is to get an array of new products and services to the markets and figure which ones work—and make a course correction. Meanwhile, Fisher is counting on a revolutionary new film-and-camera system to expand the consumer photography market. Developed in partnership with five Japanese companies, including Fuji, Canon, and Nikon, the Advanced Photographic System (APS) is scheduled for launch in early 1996. Its drop-in film cartridges will eliminate the

problem of misloading. More important, APS cameras will digitally record information such as shutter speed and aperture on a magnetic strip running across the film spool. That data will help a new generation of photo-processing gear churn out better prints.

Based on the growth spurt that accompanied prior new film standards, such as the Instamatic, 110, and Disc formats, Kodak sees a nice uptick in film and camera sales. But with heavy investment needed to start APS production, it's less certain that profits will surge as quickly. APS could displace higher-margin, traditional 35mm sales. Another dan-



DIGITAL DEVELOPMENTS

To lift Kodak's stature in electronic imaging, Carl Gustin plans to roll out a new digital camera and resurrect the Photo CD project

ger: Kodak developed the Disc and 110 film standards itself. This time, it will be in a foot race with the Japanese.

Still, as he demonstrated at Motorola, Fisher isn't afraid of Japanese competition. Indeed, he has made expansion into Asia

Cover Story

and developing markets, often dominated by Fuji, another top priority. That reflects his view that Kodak, which has close to half of the global photography market, has missed big growth opportunities outside the U. S. "For some reason, and I don't fully understand why, we went to sleep," says Fisher. Kodak won't discuss details of the new market push, but Fisher has already made three trips

to China. And he appointed one of Kodak's most senior executives, Executive Vice-President William Prezzano, to head a new thrust into China, Taiwan, and Hong Kong.

It's all part of the broad transformation Fisher believes is finally taking hold at Kodak. In a recent speech to a group of employees, he concluded with this quote from Niccolò Machiavelli's *The Prince*: "There is nothing more difficult to take in hand, more perilous to conduct, or more uncertain in its success, than to take the lead in the introduction of a new order of things." Or, he added, more invigorating. But then, if Fisher didn't want a challenge, he would still be chairman of Motorola.

By Mark Maremont in Rochester, N. Y.

THE TIMES OF YOUR LIFE—AS MANY TIMES AS YOU WANT

It was a classic Kodak moment: A photo of my father carrying my three-year-old daughter on his shoulders, framed by the colors of a New England autumn. Naturally, I had misplaced the negative. No matter. Standing in front of a new Kodak CopyPrint Station, I slipped my snapshot into something resembling a small photocopier. I pushed a few buttons on a touch screen, selecting two 5x7 prints. Five minutes later, the copies came out of a nearby thermal printer. To my untrained eye, they were nearly perfect duplicates.

Introduced in the U. S. in July, the CopyPrint is Eastman Kodak Co.'s boldest attempt to apply digital imaging technology to amateur photography. And it's getting rave reviews. Atlanta-based Wolf Camera Inc. installed 70 of the \$27,000 machines in its stores in early November. And consumers seem willing to pay a little extra for the instant gratification: An 8x10 CopyPrint enlargement retails for about \$10, compared with \$7 normally. "It's the biggest hit we've had in years," says President and CEO Charles R. Wolf. Most Wolf Camera stores have at least doubled enlargement sales, he says, and some have had a fivefold increase.

OFF THE SHELF. In the past, Kodak has tried to boost sales by encouraging people to take more pictures. But that ignored a vast, untapped market: the 98% of photos that are never copied or enlarged. The company hopes to change that by making it easier and more enjoyable for consumers to copy their photos and use them as gifts. It's also betting that

the easier enlargement process could lead to more picture-taking—and to big sales of the special paper and dyes used in CopyPrint machines.

The idea for the CopyPrint station originated back in 1993, before the arrival of CEO George M. C. Fisher. Market research showed that many consumers don't make enlargements because they've lost their negatives, or they simply don't want the hassle of dropping off and picking up an enlargement order that can take days to fill.

Befitting the company's new flex-

quadrupled its weekly enlargement business, to about 80 orders. Many were treasured family portraits being copied by people over 55 who had long ago lost the negatives. Kodak says several thousand machines will be installed around the world over the next couple of years but won't provide any detailed information.

One drawback is that the CopyPrint Station allows only limited manipulation of images, such as simple cropping. But Kodak began selling a \$40,000 Digital Enhance-



ibility under Fisher, managers moved quickly by buying off-the-shelf components to build the CopyPrint Station. The machine's scanner, which transforms a photo image into digital bits and bytes, is made by Epson. It also uses a Sun Spare microprocessor and workstation to help manipulate the information. Kodak contributed a high-quality thermal printer and proprietary software to ensure true color reproduction.

The new product was test-marketed in Perth, Australia, in early 1994. Results far exceeded expectations: The average shop nearly

ment Station in November that has far more features. Intended for use behind the counter by photo retailers, the costlier product can correct flaws such as red-eye. And it can turn prints into gifts, such as greeting cards and mock magazine covers. Kodak promises more to come, including a \$69,000 machine, due out in April, that will allow consumers to do much of this themselves.

Nobody's more excited about the enlargement products than Fisher. "It's a striking example of how we can show consumers they can do a lot more with their pictures than shove them in the shoebox." In the process, Fisher wants to milk that Kodak moment as many times as possible.

By Mark Maremont
in Rochester, N. Y.

DUPE-IT-YOURSELF

So far, Kodak's CopyPrint enlargement stations are a smash



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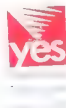
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REGULATION

IS THE FDA HOOKED ON CAUTION?

It faces fresh wrath from the right, which sees excessive regulation and slow approval

When his heart needed help a few years ago, Peter A. Chevalier shouldn't have had any trouble getting the most advanced pacemaker. He was then a research and development chief at Medtronic Inc., a leading medical-device maker. Although the company's newest pacemakers were on sale in Europe, the U.S. Food & Drug Administration hadn't approved them, forcing Chevalier to use an older, inferior model. Now, says Chevalier, the FDA is holding up approval for Medtronic's latest device, which offers a better method of adjusting heart rates based on the body's needs. "In an attempt to eliminate all risks, the FDA is delaying the entry of new technology," he fumes. "We have a situation bordering on a crisis."

Chevalier's is just one voice in a chorus of criticism being leveled at the FDA these days. Conservatives charge that the agency and its activist chief, David A. Kessler, have let thousands die by not approving lifesaving drugs and devices fast enough. GOP lawmakers vow to take a close look at the FDA, which regulates one-quarter of the U.S. economy. "There will be an effort to look at the agency and say: 'You've failed the American public in many ways. Come in and justify yourself,'" warns Representative David M. McIntosh (R-Ind.), chairman of a new government reform and oversight subcommittee on economic growth and regulation.

FROZEN AINT "FRESH." Some on Capitol Hill are considering an overhaul of how the \$970 million agency works. Among the most radical ideas: no longer requiring proof that drugs are effective as well as safe, and farming out product approvals to private organizations, as some European nations do. Some would let just about any drug or device be sold without agency review as long as it's labeled "not FDA-approved."

At the very least, say many industry executives, Congress should rethink the FDA's role as both an enforcement and

Kessler's stepped-up enforcement may be taking resources away from product reviews. "Protecting the public health means approving new drugs as fast as possible—rather than devoting massive resources to go after the word 'fresh' on [frozen] orange juice," says Kenneth P. Berkowitz, recently retired vice-pres-

“There is a clash between the right of the individual [to get any drug] and the duty of government to prevent harm”

—DAVID A. KESSLER
FDA Commissioner

ident at Hoffmann-La Roche Inc.

The odds of radical change are slim, however. The FDA points out that ever since the thalidomide disaster more than 30 years ago, Congress has demanded that the agency ensure that drugs are both highly safe and effective.

The key question is whether or not to change how the agency balances risks and benefits. Should the FDA go further in allowing greater risks for drugs and devices that could be the only hope for

Should it give doctors more latitude deciding whether treatments work?

Such trade-offs may have their price. Consumer advocates and even some drug companies are nervous about an effort to weaken the FDA's vetting procedures. "The very high standard of FDA review gives the medical commu-



nity confidence in prescribing drugs, thus boosting sales, explains one biotech executive. GOP politicians realize that if they alter this balance or weaken FDA oversight, they risk being blamed for future disasters. No one wants a disaster like the 1989 generic-drug fiasco when drugmakers repeatedly deceived and bribed—a weak, toothless agency.

While the debate over standards goes on, FDA defenders note it is already responding to long-standing criticism

...er declined to be interviewed. But officials say the agency is on target to meet 1997 goals of slashing review times from 2½ years to less than 1 year for all drugs thanks in part to 1992 legislation that lets it charge for applications. "By 1997, industry will realize that drugs are approved faster here than anywhere else in the world," says an FDA official. Even some industry executives agree that the agency should be bashed for all delays and rejections. "If something is no more effective than a placebo and a company spends millions on trials to find that out, that's the FDA's fault," says Ascher Sulowitz, chief executive of device maker NeoVision Corp.

FASTER, FASTER. Still, critics aren't satisfied. Executives charge that the FDA is obsessed with minimizing risk, keeping products off the market (table). And to speed up approvals, the agency is asking for more clinical data before the review clock

at Washington University in St. Louis.

To some critics, nothing demonstrates FDA foot-dragging better than the chicken-pox vaccine Varivax. Since 1981, this vaccine has been tested safely on more than 10,000 people in the U.S. Since 1984, 2 million children in Europe and Asia have had versions of it. Yet Varivax is still lumbering through the FDA.

An FDA advisory committee first recommended approval in January, 1990, a year after Merck & Co. sought the O.K. Early last year, a second panel pronounced Varivax safe and effective. The Centers for Disease Control (CDC) and the American Academy of Pediatrics both urge universal use.

Yet the FDA is unapologetic about its tough stance. Data from 20 years' experience in Japan and elsewhere show that as many as 2% of inoculated children develop mild cases of chicken pox, a higher failure rate than other childhood inoculations. Regulators also worry that—years later—Varivax might spawn

Alzheimer's drug tacrine, sold under the brand name Cognex. There's no other drug to treat this debilitating disease, which affects 4 million Americans. But for seven years, the agency refused to clear tacrine, prompting protests from victims, doctors, and families desperate for anything that will help. Officials reply that it took years to show even a minuscule benefit and that the drug has serious side effects. "There is a clash between the right of the individual [to get any drug] and the duty of government to prevent harm," Kessler said in a 1992 speech defending the delay on tacrine. He added it would be "foolish" to put "useless drugs" on drugstore shelves just to push products out faster.

DISMAYED. But criticisms from drug-makers pale before complaints from the medical-device industry, which lacks the pharmaceutical companies' long history of FDA scrutiny. Virtually unregulated until 1976, such devices were examined only for engineering performance, not clinical results, through most of the 1980s. Inevitably, defective heart valves and other devices reached the market. And when questions arose about the safety of others, such as breast implants, Kessler learned to his dismay that the agency's Center for Devices & Radiological Health had no data on them and couldn't answer questions from Congress about the products' safety.

Under pressure from both Kessler and lawmakers, the device-review process ground to a halt. What's more, the agency and Congress had raised the bar for new approvals. Under the Safe Medical Devices Act of 1990, most devices need to show only that they are "substantially equivalent" to products already on the market. But the law also allows the agency to ask for some safety and efficacy information if the device contains new technology. The industry charges that the FDA is using this provision to require far too much evidence. "It's not the role of the FDA to determine relative efficacy," says Medtronic's Chevalier. Instead, he says, decisions about which products work better "ought to be made by the medical community."

The FDA's more exacting standards have been a blow to an industry made up mostly of small companies. "Studies have had to be larger and longer than in the past," complains J. Casey McGlynn, a Silicon Valley lawyer who specializes in technology issues. That has driven up the cost of developing truly novel devices from \$25 million to \$75 million since 1990, says Medtronic CEO William W. George, citing industry figures. The rising expense has driven

The FDA Under Siege

Conservative critics charge that FDA red tape is killing industries—and people—by keeping valuable products off the market. Here are some of the cases they cite—and the FDA's response:

CRITICS CHARGE...

THE FDA RESPONDS...

The FDA should have prevented thousands of heart-attack deaths by approving tests of the "cardio-pump," used for CPR.

The pump may not work any better than ordinary CPR. And there's no way to get the victim's consent.

Alzheimer's victims suffered when the FDA took seven years to approve tacrine.

The drug has severe side effects. Years of testing showed limited efficacy.

By not approving the Sensor Pad to help detect breast lumps, the FDA placed thousands of women at risk.

The pad may actually make detection more difficult, and the company hasn't done the necessary trials.

Chicken pox vaccine, under development for 21 years, is still not approved by FDA.

The vaccine might have long-term detrimental effects. Besides, chicken pox is not a deadly disease.

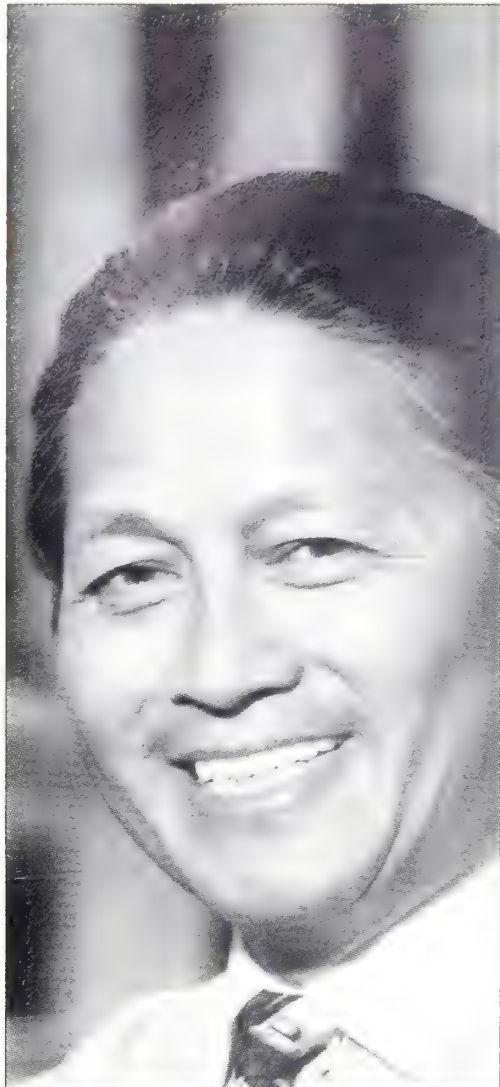
Advanced pacemakers are available in Europe, but not in the U.S.

Benefits of the new device are still not established.

...ts ticking, they say. That actually lengthens the time between the start of development and submission to the FDA. A Tufts University study of FDA approvals from 1990 to 1992 shows that the review time for important drugs averaged only 20 months, compared with 31 months for all drugs, development time for these key products was 18 months longer. "The FDA process is

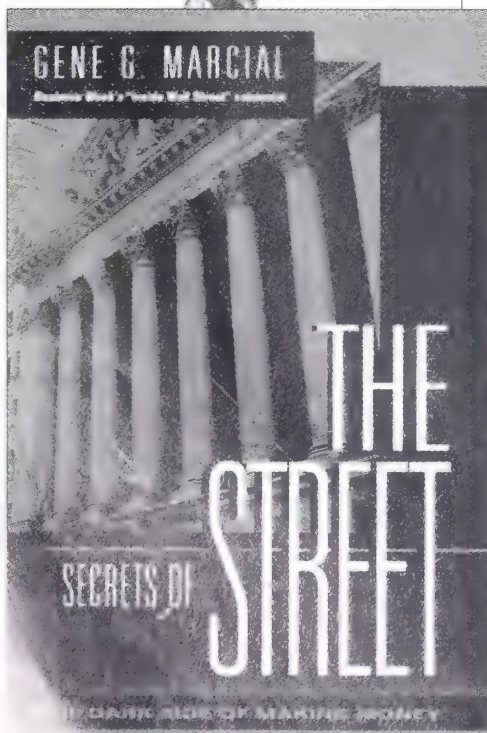
adult cases of the disease or trigger related viral conditions, such as shingles.

Varivax offers a classic example of the FDA's juggling act. How should regulators assess risks, and who should make the final decisions? "The FDA believes it knows best how to strike this balance," says Alan M. Slobodin of the conservative Washington Legal Foundation. "But maybe it's better for pa-



A CANDID, DRAMATIC EXPOSÉ THAT TAKES YOU TO THE DARK SIDE OF MAKING MONEY

From the quintessential insider, Gene Marcial, *Business Week's* "Inside Wall Street" columnist.



"It's easy when you know how. It's easy when you're connected. It's easy when you've helped someone else with the well-timed tip to receive another in return. It's easy when there are so many good companies and so much information and so many people and so much sheer greed." — GENE MARCIAL



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make the U.S. climate more hospitable rallying powerful allies such as House Speaker Newt Gingrich (R-Ga.) to their cause. Gingrich, who has called Kessler "a bully and a thug," has also blasted the agency for refusing to allow tests of a pump, available in Europe, designed to make cardiopulmonary resuscitation more effective. He insists that Americans are dying unnecessarily because it's not available here. But researcher Michael Callahan of the University of California at San Francisco says that there's no firm evidence so far that the pump in question works better than standard CPR. And the FDA is reluctant to permit tests—because the patients who are unconscious, cannot give their consent.

The coming months promise pitched battles on all these issues. Even within the FDA, there's an argument going on over whether the reviews for thousands of simple, noncontroversial devices such as tongue depressors might better be

Gingrich calls Kessler "a bully and a thug" and gripes he blocked tests on a pump

farmed out to private organizations.

Any significant change to the FDA's standards, mission, or responsibilities, however, would require new legislation. And so far, the agency's Republican critics haven't begun to discuss what changes—if any—they really want to make. Indeed, Congress' most recent actions, the 1990 Medical Device Act and a 1994 dietary supplement bill, moved in the direction of stricter regulation. What's more, some AIDS activists say the agency has been approving some drugs too quickly, without enough clinical testing to figure out the best way to use them, or even if they work. Outside the Beltway, says Kenneth I. Kaitin, deputy director of Tufts University's Center for the Study of Drug Development, "there's now less attention on increasing drug availability and more attention on protecting the public."

Once again, the FDA may get caught in the middle. And just as Congress did in 1990, lawmakers will have to grapple with a very hard question: How will patients be served best?

By John Carey in Washington, with Joseph Weber in Philadelphia and Joan O'C. Hamilton in San Francisco

EDITED BY PETER COY

HORMONE CHECK-UP FOR SENIORS?

NEW HORMONE-REPLACEMENT therapy appears to ease the pains of aging. It involves an adrenal-gland hormone: dehydroepiandrosterone, or DHEA, which usually dwindles by age 70 to about 10% of its peak at age 20. Dr. Samuel S. C. Yen, an endocrinologist at the University of California at San Diego, gave daily pills of synthetic DHEA to 13 men and 17 women aged 40 to 70. He reported his research last year in the *Journal of Clinical Endocrinology & Metabolism*. The results: 50% of the women and two-thirds of the men in the double-blind study reported "increase in well-being," more energy, and less muscle fatigue. Sexual desire appeared to be unaffected. DHEA was discovered in 1950 by French scientist Etienne-Emile Baulieu, who also created RU-486, the abortion pill. Although DHEA's precise function remains uncertain, Yen's findings "make sense," says Alberto Hayek, an endocrinologist with the Whittier Institute in La Jolla, Calif. Larger clinical trials are planned, and Yen says he expects the market DHEA.



YABBA DABBA DON'T SWIPE THIS TOON

FRED FLINTSTONE NOTWITHSTANDING, HANNA-BARBERA Cartoons Inc. is no Stone Age studio. To guard against counterfeits of its celluloid images—which fetch \$750 and up in the collectors' market—Hanna-Barbera is employing the very latest in biotechnology. First, the studio snips some hair from the head of 83-year-old co-founder Joseph Barbera. Using a technique called polymerase chain reaction, it isolates a fragment of Barbera's DNA, then makes millions of copies of it. These copies are mixed into a special ink used for Barbera's signature and a numbered seal, both of which go on the celluloid frames, known as cels. A handheld scanner can instantly read the genetic ink, verifying the signature and checking the seal against a database of registered cels. Co-founder William Hanna, 84, uses conventional ink for his co-signature.

Hanna-Barbera's development partner, Los Angeles-based Art Guard International Inc., has big plans and a patent for the DNA marker technology. Art Guard President Charles Butland says it could protect items ranging from paintings to coins to credit and I.D. cards.

MAKING A PAGER FROM ISRAEL'S ARSENAL

NEXUS TELECOMMUNICATION systems Ltd. in Tel Aviv has invented a low-cost system for two-way paging based on Israeli military communications technology. A subscriber creates as many as 300 possible messages in advance and stores them in the paging-company's computer, assigning each a number. To respond to a page, the subscriber simply scrolls through a list of printed messages on the

pager screen and transmits back the appropriate number—say, 124 for "I'll be there in 20 minutes." The paging-company computer translates the number and forwards the message by fax, E-mail, or by phone using a synthesized voice.

Having to choose from a list of predefined messages is limiting, but the offsetting advantages are huge. Nexus' NexNet messages are so short that the pagers need

less than a watt of power to send them, and the low power lets the pagers transmit in a free, unlicensed portion of the U.S. airwaves. To cope with the electromagnetic "noise" in that crowded spectrum, Nexus uses a frequency-hopping method that was developed to be virtually immune to enemy jamming. American Paging Inc. in Minneapolis is co-developing the system for the U.S. market, while Samsung Electronics Co. will manufacture the two-way pagers.

THE LAB WHERE MADAME BUTTERFLY MEETS MR. CHIPS

CHIP RESEARCHERS AT TUFTS University have shed light on how butterflies trap heat from the sun. Now, they hope lepidopterists will return the favor with some insight into chip fabrication. The common element in both problems is the way infrared radiation interacts with thin films. In 1992, Tufts researchers under the direction of Engineering Dean Ioannis Miaoulis discovered that weird things happen to silicon wafers when the films they're made of are about the same thickness as the wavelength of infrared radiation, a form of heat. They found that tiny varia-



tions in film thickness cause the heat rays to bounce around, forming tiny hot and cold regions that can damage the wafers.

Miaoulis, graduate student Bradley D. Heilman, and others then looked for parallels in the animal kingdom. They discovered that the thickness and spacing of microscopic films in the scales of butterfly wings were just right for absorbing heat from the sun. Now, they want to know if the roughness of those wing scales helps even out hot and cold spots in the wings. Such an insight could help in chip fabrication. That's where the Tufts group hopes lepidopterists can pitch in. Says Miaoulis: "We're operating in the crevices between fields."

DERIVATIVES: ALIVE, BUT OH SO BORING

Yesterday's shooting stars are today's low-margin mules

The last decade has not been kind to commercial banks' product lines, which have come under fierce attack by nonbank competitors. As a response, during the late 1980s, a few of the most venturesome banks perfected a shiny new product with a wondrous profit margin: the derivative. Soon, many investors and corporations were using them for hedging risks and betting on interest rates and currencies. Dozens of other banks rushed in, and the number of derivatives dealers mushroomed between 1988 and the end of 1993.

Now, though, the once wondrous margins are shrinking fast. A slew of multimillion dollar hits taken by corporations and institutional investors has caused many users to run for cover. Demand for the most exotic derivatives contracts—those that are most lucrative for dealers but often carry the most risks—has plummeted. Many users now limit themselves to the safest derivatives, those least profitable for dealers. "The only thing people are buying these days is Chevys," says Bruce L. Campbell, associate director of corporate derivatives marketing at Fuji Bank & Trust Co. "They don't even want to see a Maserati in the showroom window."

STILL HANDY. Derivatives will not go away. Too many corporations and investors view them as useful, indeed critical, risk-management tools, and experts expect derivatives activity to continue to expand at a healthy pace. But they agree that the days of outrageous profitability for dealers are over. With corporations and investors still licking their wounds, traffic in the most complex derivatives will likely stay slow for some time. "The structured-note market will continue to exist," says John K. Darr, finance director of the Federal Home Loan Bank system, referring to the intricately structured instruments that are a big part of the complex derivatives market. "But it may be somewhat slower than it was."

Moreover, with the proliferation of

derivatives dealers, it will be difficult if not impossible for the preeminent ones to retain a lock on the market, especially for complex, exotic derivatives. Inevitably, as profit margins shrink, making money in derivatives will depend more on volume than spreads—just as in dozens of other bank businesses.

In the halcyon days of the market, derivatives were a dealer's best friend. Citibank and, later, Bankers Trust and J.P. Morgan were the dominant U.S. banks in the business and produced huge returns. As more complex derivatives were developed, banks with the product know-how could book a return on equity in excess of 100% on some of the more exotic derivatives.

But the bond-market rout of 1994 changed all that. Big hits were taken by Procter & Gamble Co., Gibson Greetings Inc., and other corporate derivatives users, many of them clients of Bankers Trust New York Corp. Several of the losses quickly led to lawsuits.

The market tumult has hurt all dealers in derivatives. J.P. Morgan's derivatives-trading revenue was down 17%, to \$663 million, for the year. Citibank's was down 50% for the first nine months of 1994. And Chase Manhattan Corp. took a fourth-quarter loss of nearly \$20 million on several derivatives contracts. But Bankers Trust, arguably the preeminent bank in derivatives, has been the most vulnerable. Indeed, its fortunes have been something of a mirror



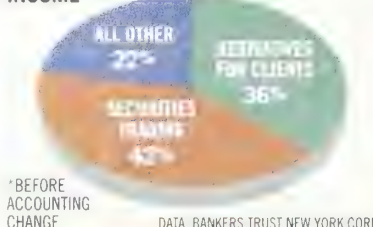
for the derivatives turmoil. "They're a one-trick pony," says one dealer.

Nearly a third of Bankers' 1993 net income of \$995 million came from derivatives, and with derivatives dealers' margins high, Bankers produced a handsome 26% return on equity. But beginning in the second quarter of 1994, income from derivatives fell sharply. One key reason: Bankers Trust specializes in the most complex derivatives, the segment of the market that dealers and consultants agree has slowed the most.

The slump is literally scaring some dealers away. Charlotte (N.C.)-based First Union Corp. was gearing up to start dealing in structured notes, a type of complex derivative, in early 1994, but activity was off so much, the bank decided to wait, according to Terry L. Turner, managing director of its derivatives group. "The whole idea of leverage [and exotic derivatives] for many investors is out," says Heinz Binggeli, managing director of Emcor Risk Management Consulting. "We're getting back to prudent hedging rather than yield enhancement." Market sources say as much as half of the limited activity in

DERIVATIVES-DEPENDENT

BANKERS TRUST'S INCOME* JAN., 1993, - SEPT., 1994



complex derivatives in 1994 was transactions aimed at reversing old trades. Worse, thanks in part to the spate of customer lawsuits and complaints, Bankers Trust is losing some market share in exotics even as that market grows. A survey of dealers by the magazine *Risk* shows that in mid-1994, Bankers Trust dropped in rankings in

management field when we come up with strategic solutions to problems" rather than simply try for a lot of transactions, says Charles S. Sanford Jr., chairman and chief executive of Bankers Trust. In December, Bankers merged its equities sales force and its equity derivatives sales force, a move that sources say could lead to a more integrated approach to clients. Market sources say an internal restructuring of its deriva-



derivative markets for complex derivatives. It's not as if Bankers Trust—or any other dealer—can easily generate profits in the more prosaic end of the market. Today, margins on everyday interest-rate swaps are down to a few percentage points. Bankers Trust, whose derivatives business has been very transaction oriented, is now trying to build longer-term relationships with clients that will eventually produce more high-margin business. "We can do more in the risk-

derivatives business is also in the offing, though a Bankers spokesman declined comment as a matter of policy.

Certainly, Bankers Trust has proven it can change its stripes. In the late 1970s, then-chairman Alfred Brittain III decided to exit retail banking. The bank sold its branches and its credit-card portfolio and grew into a capital-markets powerhouse—a transformation like no other bank's. "We like to think of ourselves as a change-agent, innovative type of firm," Sanford says. "I would hope we'll be in a transformation for the next 10 years."

Change of the kind Bankers Trust is contemplating can take time, though. Says Thomas C. Theobald, former chairman of Continental Bank Corp.: "This is multiyear if not decade-long stuff to move a cultural positioning. You can't flip-flop in a year or two."

In the meantime, Bankers has to deal with a competitive handicap. After Gibson Greetings sued it over derivatives losses, the Federal Reserve Board looked into Bankers' derivatives sales practices and eventually reached an agreement with the bank that publicly called for it to modify them. Among other things, Bankers Trust must now give many clients daily prices on their derivatives. Customers receiving that information can use it to bargain for lower prices or share it with other dealers, giving them insight into Bankers' transaction structures. Already, savvy customers of all dealers make a habit of shopping around for transaction prices. A Bankers spokesman says he does not expect the requirement to hurt the bank.

DON'T RUSH. While Bankers Trust tries to revamp, its biggest competitors are pushing hard to win market share. U.S. rivals including J.P. Morgan and Chase Manhattan as well as foreign threats such as Swiss Bank Corp. are making inroads. At Bank of America, "over 25% of our client base were new users of our services last year," says Joseph P. Bauman, senior vice-president and director of the bank's global derivatives business.

Few see Bankers hobbled indefinitely. But derivatives profits are not likely to reach old peak levels anytime soon, says Arthur Soter, a bank stock analyst at Morgan Stanley & Co. He expects Bankers to generate only \$240 million in derivatives income in 1995, well below 1993's \$330 million.

For Bankers and other banks, the lesson of the derivatives debacle is clear: Rushing into seemingly miraculous markets is not a recipe for long-term success. In today's financial markets, high-profit products tend to have distressingly short life cycles.

By Kelley Holland in New York

End Of The Windfall

NEW PLAYERS have entered the market, and they are aggressively competing on price to win market share and clients. There is even more competition for the most complex deals, long the province of a few dealers. That is reducing once lofty margins on deals.

Wary customers and heightened competition mean profits for derivatives dealers will be more elusive in coming years

EXOTIC DERIVATIVES BUSINESS has slowed thanks to unsettled capital markets and well-publicized losses by sophisticated users. Market sources say activity in the most complex derivatives is off by a third or more. Many users are confining their dealings to conservative, risk-limiting moves using plain-vanilla, low-margin derivatives.

NEW DISCLOSURE REQUIREMENTS could force users to report on all their derivatives, even if used as hedges. Dealer profits might be hurt if aversion to this leads investors and corporations to limit use of derivatives. Dealers may also be pressured to disclose more information on how they price derivatives, which could cut further into profits.

THRIFTS

RISKIER AND RISKIER AT THE HOME LOAN BANKS

The federal system's new investment strategy raises eyebrows

Back in the darkest days of the Depression, New Dealers devised a clever way to prop up the devastated housing market: a network of government-sponsored banks that would lend funds to capital-starved savings and loans. Flush with cash from the new Federal Home Loan Bank system, thrifts could lend once again. During the following decades, housing ownership expanded exponentially.

But the once noble mission of the 63-year-old bank system is becoming an anachronism. To be sure, the 12 FHLBs have more than \$100 billion in low-cost funding outstanding to thrifts as well as those banks that choose to become members by investing in the system. But these days, the dominant role by far in recycling mortgage money is played by the huge \$1.5 trillion secondary market for home mortgages. Meanwhile, the FHLBs' once powerful regulatory authority over thrifts has been assumed by the Office of Thrift Supervision.

HELPING HAND. The FHLB system, though, is likely to escape extinction because of a more recent *raison d'être*, little known beyond Capitol Hill, that has nothing to do with its original mandate: helping to clean up the 1980s savings and loan mess. Under 1989 legislation, the FHLBs, and indirectly, their members, pay \$300 million annually for interest on S&L cleanup bonds, about 8% of the total interest tab.

But critics are increasingly worried about how the FHLBs are paying that bill, as well as dividends to members. The banks have been using complex financing techniques, including billions of dollars' worth of "structured notes," volatile debt securities whose yield is linked to such indexes as interest rates.



HAMM: Worried insider

Some of those notes ended up in bankrupt Orange County's portfolio. John K. Darr, director of finance for the FHLB system, says all investors were warned of their riskiness.

Another FHLB tactic to boost earnings: borrowing money cheaply via bonds and notes, thanks to an implicit government guarantee, and investing some proceeds in higher-yielding mortgage securities. That produces a hefty arbitrage profit. The FHLB system's investments swelled from \$33.9 billion at the end of 1989 to \$90.5 billion at the end of 1994's third quarter. While the banks have managed these investments well so far, some have been taking such steps as extending the maturity of their portfolios to produce higher earnings. But that has increased the exposure of their capital cushion to interest-rate moves.

The ballooning investment portfolio

Some critics see little use for the FHLBs altogether. In a 1993 report, the Congressional Budget Office noted that because of the secondary-mortgage market's growth, policymakers ought to consider whether the government should continue to offer subsidized liquidity, especially since most loans don't go to low-income homeowners. "We have cut the subsidy bandwagon at some point," says banking consultant Bert El

FHLB defenders say that for smaller institutions that hold on to their mortgages and for mortgages that don't meet the criteria for resale in the secondary market, the bank system is a lifeline. "It's awfully hard for a small institution to find viable low-cost sources of funds outside the Home Loan Bank system," says David F. Hollander, CEO of Boston Federal Savings Bank, which has assets of \$675 million.

LITTLE LEEWAY. And defenders dismiss worries about the system's soundness. Despite gyrations in interest rates last year, the banks' net income through the end of the third quarter rose 7.4%, to \$739 million. FHLB of Boston President Michael A. Jessee contends that the system's regulator, the Federal Housing Finance Board, closely monitors investment policies. "There is just not a lot of leeway to take on excessive risk," Jessee says.

While the FHLB system is not on the GOP hit list, it is coming under scrutiny in Washington. Representative Richard H. Baker (R-La.), chairman of the

House Banking subcommittee with oversight responsibility for the FHLB system, is expected to introduce legislation soon that would assure minimum capital levels. Capital levels shrank in the 1980s when Congress tapped the system's healthy balance sheets for a \$3.2 billion contribution to the S&L cleanup. Deputy Treasury Secretary Frank N. Newman has said the Administration will draft its own reform proposal.

Neither of these measures is likely to call for abolition of the Federal Home Loan Bank system. And with its crucial role in quietly paying off one of Washington's most embarrassing blunders, the FHLB system won't have to do much to justify its existence. If the system gets into trouble, however, Washington may have second thoughts.

By Amy Barrett in Washington

Do We Need The FHLB?

YES

The FHLB system encourages lending to borrowers, particularly low-income homeowners, who don't fit the cookie-cutter mold required to sell mortgages in the secondary market. It also lends to member thrifts with liquidity problems. This allows them to put more money to work making mortgage loans.

NO

The advent of the secondary market for mortgages and increasingly efficient capital markets for even smaller financial institutions make the FHLB's lending activities increasingly redundant. And many loans by FHLB members go to wealthy homeowners, not low-income borrowers.

DATA BUSINESS WEEK

concerns some Clinton Administration officials. Says one: "If mismanaged, there is a risk to the taxpayer." Even some FHLB officials worry about the arrangement. "Our business is not to be in arbitrage," frets William G. Hamm, chief operating officer of the San Francisco Federal Home Loan Bank. "But that [interest-payment] obligation has made it our business."

**STALLINGS: ZERO
EXPERIENCE IN A
CUTTHROAT FIELD**



MUTUAL FUNDS

S PILGRIM MAKING ANY PROGRESS?

New owner Robert Stallings says its ailing funds are treatable

has been one tough year for the mutual-fund industry. But you haven't seen real trouble until you look at Pilgrim Group. Last year, it was tarred by scandal: Pilgrim and CEO Patricia Weingarten were sanctioned by the National Association of Securities Dealers and paid fines for misleading advertising. And its funds performed poorly: Assets dwindled to just \$1.7 billion at yearend 1994 from \$3 billion in 1992. By late last year, Weingarten decided to sell the fund company. Now, it's Robert Stallings to the rescue. To be sure, the 45-year-old mortgage banker and his Scottsdale (Ariz.) Express America Mortgage Corp. seem like unlikely saviors. Express America itself has been bleeding red ink for two years. And Stallings has no experience with mutual funds. Still, he's ponying up \$28 million to buy seven of Pilgrim's funds, with some \$1.15 billion under management. He's even keeping the Pilgrim name and has moved to Los Angeles to be close to the operation. Stallings insists he can restore Pilgrim to health. Others aren't so confident. "It's going to be an uphill battle," says Don Phillips, publisher of *Morningstar Mutual Funds*. "Why in the

world would they even want to try?" Weingarten declined comment.

Stallings argues that Pilgrim is a virtual gold mine. He says its two closed-end funds will produce steady cash to help rebuild the company. Like mutual funds, fees for closed-end funds are based on assets under management. But unlike mutual funds, unhappy shareholders can't take their money out. They can only sell the shares for whatever they fetch in the market. Pilgrim Prime Rate Trust, with \$720 million in assets, and Pilgrim Regional Bankshares, with \$156 million, should produce more than \$7 million a year in fees. And Stallings considers Pilgrim MagnaCap Fund, with its market-beating 4.1% total return in 1994, "a great lead horse" for a family of equity funds.

But the closed-end funds may not be the cash cows he's counting on. Both funds, listed on the Big Board, trade at deep discounts to their net asset value (NAV). But shareholders of Pilgrim Regional Bankshares have the right to vote on whether to con-

vert to a mutual fund—and the betting is they'll do it in 1996. That will open the door to redemptions.

Prime Rate Trust, trading at 13% below NAV, has no such provision, but it poses problems for Stallings, too. To boost share prices, he may have to launch a buyback, which would shrink the assets. If that doesn't improve the share price, it could invite a hostile raid that could wrest control from Pilgrim, says Robert Grunburg, former Pilgrim Group president.

WEAK RECORD. Can Stallings improve the lot of Pilgrim fund shareholders? He hasn't done much for his own. Stallings took Express America public in 1992 at \$10 a share. The stock soared to \$16 in 1993 as the company rode the mortgage-financing boom. Since then, Express America has racked up nothing but losses. Stallings cleared \$45 million from the sale of the mortgage-servicing business last summer. The stock now trades at around 4.

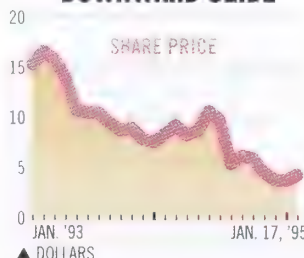
Even the sale to Express America—which is subject to the approval of the acquired funds' shareholders—won't end Weingarten's woes. She'll still be saddled with 10 unsaleable adjustable-rate mortgage (ARM) funds. These funds, which are supposed to be little more volatile than a money-market fund, turned in disastrous losses in 1994, ranging from -12.5% to -20.5%.

Most ARMs funds invest in government-backed securities. But Pilgrim sought higher yields by investing in private-issuer ARMs. When the credit quality of some of those issuers slumped, so did the prices for their ARMs—and the NAVs of the funds. That, in turn, triggered shareholder redemptions, which forced Pilgrim to dump these illiquid securities at fire-sale prices. That further shaved NAVs, which, of course, prompted more redemptions. Even if the ARMs funds are totally liquidated, some debts remain. The funds owe millions to banks for borrowings used to advance commissions to brokers.

Even under new management, Pilgrim won't have an easy time selling its wares. Brokerage firms and financial planners who formerly sold Pilgrim funds are slashing the number of fund groups they deal with. To get distribution, Pilgrim will have to compete with titans such as Fidelity, Franklin, and American Funds. It's going to be awfully tough for a small player without any fund-industry track record to pull that off.

By Eric Schine in
Los Angeles

EXPRESS AMERICA'S DOWNWARD SLIDE



DATA: BLOOMBERG FINANCIAL MARKETS

BY GENE G. MARCIAL

CADBURY: SWEET TALK TO DR PEPPER

Recent takeover fizz about Dr Pepper/Seven-Up (DPS) may be more than just bubbles. Rumors are flying that Cadbury Schweppes (CADBY), the British confectionery and beverage outfit, is close to striking a deal to acquire Dr Pepper. Cadbury already owns 25% of Dr Pepper. Now at 28, Dr Pepper shares are worth 35 in a buyout, say analysts.

Dr Pepper CEO John Albers has come to an informal, tentative agreement with Chairman Dominic Cadbury, says one New York investment banker. People at Cadbury have made no secret of their interest in Dr Pepper, primarily a maker of soft-drink concentrates that it sells to independent licensed bottlers. But until now, Albers and his board would have none of it. In fact, Dr Pepper adopted a poison pill to discourage a buyout, and the company's board denied Cadbury a seat.

"But recently, things have turned quite cozy between the two," says the banker. A likely part of the deal, he believes, is for Cadbury to sell off the Seven-Up operation, which accounts for 30% of Dr Pepper's estimated 1994 revenues of \$765 million. The likely buyer is Triare (TRY), parent of Royal

pepper for both companies: Dr Pepper needs to expand internationally, but its resources are limited. (Volume outside the U.S. accounts for only 1% of sales.) Dr Pepper currently has 8% of the U.S. market for soft drinks. "Cadbury's financial resources and its global expertise would boost Dr Pepper's growth," says Solomon.

Analyst Bill Leach at Donaldson, Lufkin & Jenrette Securities thinks there's no way that Cadbury will not buy Dr Pepper. That was the original idea when it acquired its 25% stake in the company, he adds. "The only question is when." Leach thinks part of Albers' hesitation is the knowledge that, given Dr Pepper's strong cash flow, small debt, and low-cost operations, the stock could hit 50 in two years. The big winner in a takeover would be Albers himself: He owns 3 million shares. Even at a buyout price of 35, that's a cool \$105 million.

Dr Pepper declined comment.

ZOOMING IN ON INTERACTIVE TV

It's a tiny company. It has yet to make a dime, and it expects revenues this year of only \$5 million. But ACTV (IATV) has attracted the eye of several media giants, including Washington Post Co., which has taken a 26% stake. Tele-Communications and Turner Broadcasting System have entered into alliances with ACTV on projects that will use its interactive technology. And Fidelity Management has purchased 5% of ACTV, now trading at 3¢ a share. Just what is it that's attracting these biggies?

Small as it is, ACTV has "positioned itself to become a leading company in developing and delivering interactive-TV programming for the entertainment and educational markets," says Peter Mintz, an analyst at Barrow Street Research. ACTV's patented technology is designed to integrate with existing television and video systems to "personalize" watching. For instance, the technology would let sports fans have an instant replay, zoom in on a particular player, or pull up statistics about the game. In education, children would be able to interact with TV programs by answering questions and checking their answers.

ACTV and Turner's Educational Services unit have agreed to collaborate in producing programs from CNN's and

Turner's extensive film libraries. Tele-Communications and Turner, among others, will launch a test in Southern California early this year by hooking up 1,000 households with ACTV's interactive programming.

Investment adviser John Westergaard sees sales climbing to \$15 million in 1996 and to \$30 million in 1997, by which time ACTV should be in the black. The stock, he says, could hit 20 by then.

THE NO. 1 STEAL IN STEEL

Although Nucor (NUE) hasn't snapped back as fast as other steel stocks, some pros have been snapping it up. Nucor has languished near its low of 57, down from 72 in June. They think Nucor, one of the largest U.S. steel-makers—with annual sales of about \$3 billion—is now the industry's best bargain. One South Carolina money manager expects the company to top the Street's earnings projections this year and next, thanks to its rapid capacity expansion.

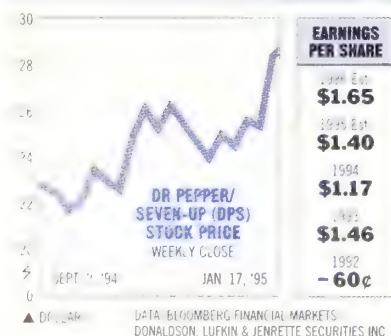
Other analysts think it will, too.

"Nucor has the best growth prospects in the steel group, with projected 17% five-year compounded unit volume growth," says Wayne Atwell, an analyst at Morgan Stanley. Based on his projected 1996 earnings of \$4.15 a share, Atwell figures Nucor could trade at 65 within a year. It is likely to remain the U.S. leader, he says, in flat-rolled steel.

Nucor operates scrap-based steel mills in seven locations. One big plus is the startup this year of a new iron-carbide plant in Trinidad. "This is a significant long-term positive," says analyst Gregg Lucas of Interstate/Johnson Lane. Iron-carbide production will insulate Nucor from volatile scrap prices and improve the quality of Nucor's flat-rolled steel, says Lucas, who upgraded his Nucor rating to a "buy."

Nucor Chairman and CEO Ken Iversen says he plans "to double the capacity of certain mills" and that production will jump to 8 million tons this year from about 7 million last year. "Orders are running strong," he says.

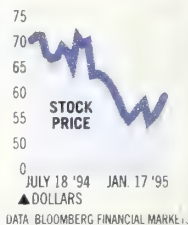
BUBBLING UP



Crown Cola, whose chairman and CEO is dealmaker Nelson Peltz.

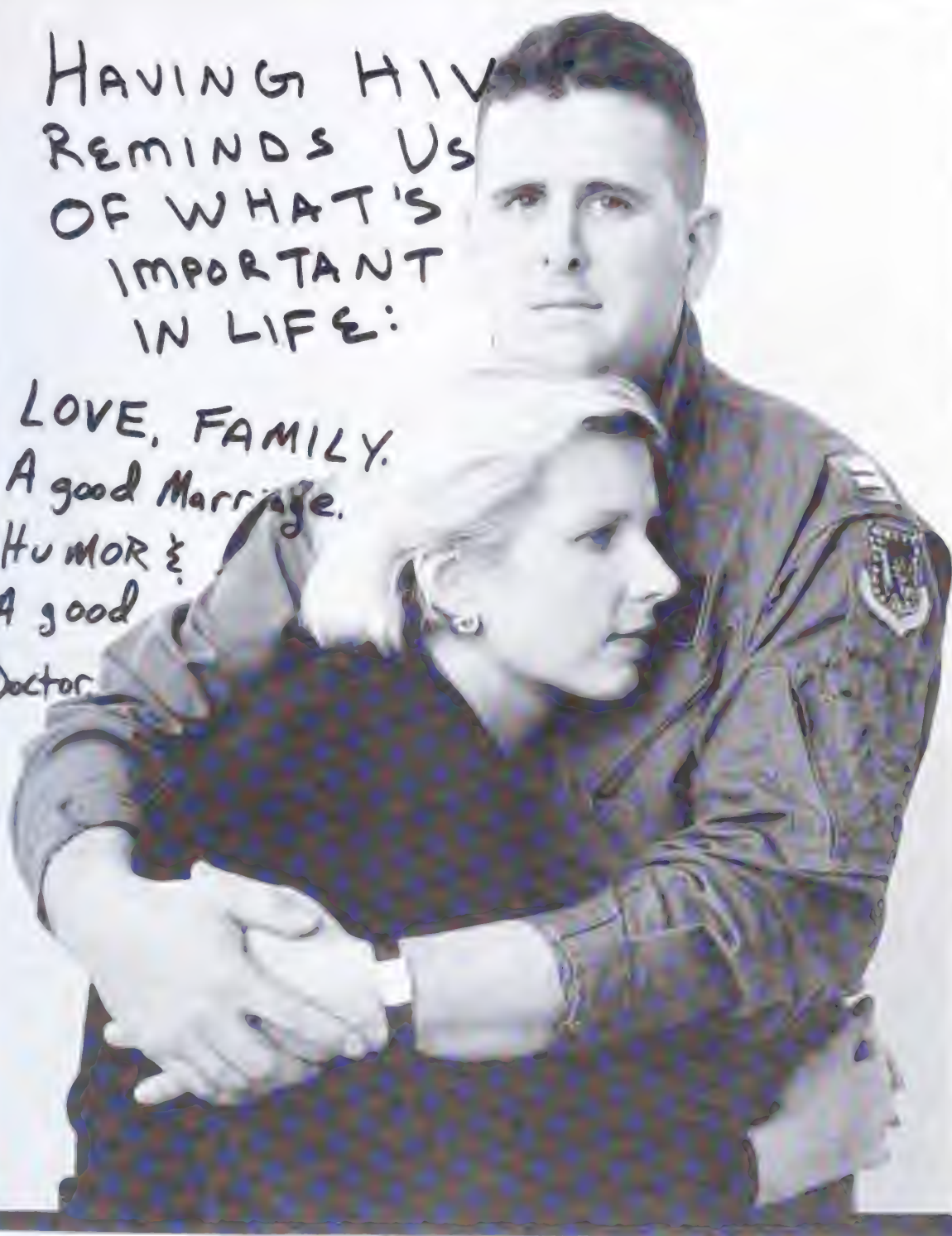
"Dr Pepper recognizes the considerable strategic benefits of linking up with Cadbury if it hopes to become a global noncola powerhouse," says analyst Jennifer Solomon of Josephthal, Brown & Ross. She says the reasons for a merger have become very com-

NUCOR FOR A SONG?



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IBM'S PARALLEL POWER RANGERS

new SP2 may ease Big Blue's mainframe dependency



WADAWSKY-BERGER: "We inherit all the hard work others have done"

How to climb the ladder at today's IBM? Be a team player, and focus on the customer. Just ask Irving Wladawsky-Berger. On Jan. 6, the 57-year-old computer scientist—dressed in a sweater for an all-day affair—was unexpectedly summoned to the Armonk (N.Y.) office of IBM Chairman Louis V. Gerstner Jr. The big news: Wladawsky-Berger was being promoted—even as Gerstner was pushing out two high-profile executives.

Gerstner stressed that it had been work and market focus that won Wladawsky-Berger the promotion. "He wanted to make sure I understand the

cultural characteristics so there would be no misunderstanding in his senior management team," says Wladawsky-Berger.

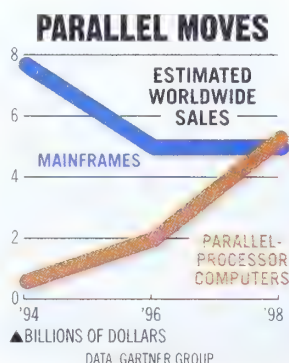
The message: Gerstner needs more IBM executives to do what Wladawsky-Berger does. In three years, he has built a thriving business around a new kind of large-scale computer—so-called parallel machines that use dozens of ordinary microprocessors and other off-the-shelf parts to deliver mainframe power in a compact, relatively easy to use, and inexpensive package.

In the process, Wladawsky-Berger's crew took innovative approaches that caught Gerstner's eye. While avoiding the "not-invented-here" syndrome that has often slowed IBM's entry into new markets, they were still good team players. They used technology that had been developed—and paid for—by other IBM units. Their SP2 system is built from the guts of IBM's RS/6000 workstation, which uses the PowerPC chip developed by IBM, Apple Computer, and Motorola. The SP2 also uses AIX, IBM's version of the UNIX operating system so that the 10,000 programs that exist for RS/6000s run on the machine. Disk drives come from an IBM group in San Jose, Calif. And technology from IBM's lab manages the system's internal communications.

PROFIT MONSTER. Hook it all together, and you have a state-of-the-art parallel computer and a tremendous profit producer. Gross margins on the SP2 are about 58%—significantly higher than the 40% IBM gets for traditional mainframes. Wladawsky-Berger's approach cuts both cost and time to market: "We inherit all the hard work others have done and then concentrate on getting to market as fast as humanly possible," he says.

Timing is everything. And the SP2 puts IBM in the right place at the right time. In fact, because the machines excel at work such as scanning huge databases, they are sparking new uses—and new demand for—large-scale computers. That's good news for Wladawsky-Berger's Power Parallel division, whose sales are expected to more than double, to around \$500 million in 1995. "In the past, you would have to go to a mainframe because they were the only things that could handle large applications," says Revlon Inc. Chief Information Officer Gene Pinadella. "But parallel computing has taken away some of the reason you would stay with a mainframe." Revlon will run North American operations on an SP2.

The success of IBM's parallel machines will take some of the sting out of the inevitable decline of conventional mainframes, a \$7 billion business for IBM. Market researcher Gartner Group Inc. estimates that the total market for such large-scale parallel machines will skyrocket from last year's \$600 million to \$5.3 billion in 1998. The new technology will then eclipse the market for mainframes, which by 1998 is expected to con-



tract to \$5 billion (chart, page 81). Analysts expect IBM SP2 sales to hit \$1 billion by the end of 1996. Already, IBM has shipped 350 machines—ranging in price from \$150,000 up to \$40 million.

For the new machines, the killer application is data-mining—the ability to quickly sift through millions of bits of data to find patterns or similarities. For example, IBM says a retail chain searching sales data with an SP2 made an interesting discovery: 28% of women who buy cosmetics also buy greeting cards. Now, that customer is making use of such findings to design a new layout for its stores—with cosmetics and greeting cards closer together.

OPEN DOORS. For John Alden Life Insurance Co., the machine is sorting through millions of medical claim forms to give management a moment-by-moment picture of the business. "Decision support is where this technology will do well," says Sullivan McConnell, director of information technology. "Getting the information faster is how we're competing in the '90s." McConnell says the SP2 finishes "in tens of minutes" tasks that took a mainframe all night.

The promise of computing power that is faster, cheaper, and more flexible is opening doors in places IBM was never welcome. Bose, the Boston-based maker of high-fidelity speakers, is one of Hewlett-Packard's biggest customers in New England. But Bose researchers wanted to use powerful software to analyze components for acoustic properties and kept running out of steam on existing computers. The best HP had to offer was a powerful parallel computer that is still in development. "IBM had a more established technology," says Dwight Schirmer, purchasing agent for Bose. "This is the first piece of equipment we've purchased from IBM, including PCs. It was a breakthrough."

IBM may, indeed, have a breakthrough product in the SP2. But Wladawsky-Berger can't do it alone. He's depending on the rest of Big Blue to keep the pieces he uses competitive and low-cost—a risky strategy, since IBM's workstation business already lags behind such suppliers as Sun, HP, and Silicon Graphics. "There is a critical link between one's workstation business and one's [parallel] business," says Greg Papadopoulos, a former Thinking Machines Corp. employee and now chief scientist at Sun Microsystems Inc.'s server unit. "The workstation business builds volume." Of course, any SP2 sales help the workstation business, too. That's the spirit of teamwork Gerstner rewards.

By Ira Sager in Somers, N.Y.



MANHATTAN TURNS INTO 'SILICON ALLEY'

How the city is snaring multimedia startups

R/GA INTERACTIVE'S STAN WINSTEN (IN MONITOR): "This is where the power is

It's a warm January evening, and a hip gallery called Here is brimming over with creative minds from software, publishing, media, and the arts. The chatter centers on opportunities in "new media": using digital technology to create new forms of interactive "content" for CD-ROMs, film, or online delivery. Silicon Valley? Seattle? Hollywood? Guess again. This is Manhattan, and the cutting-edge crowd is here for "cybersuds," a monthly get-together hosted by

the four-month-old, 500-member New York New Media Assn.

It's true: Manhattan is emerging as the gritty breeding ground for new media, earning it the dubious title of Silicon Alley. Sure, the rents are high, the suits harrowing, and the taxes crushing. But new-media businesses are flourishing. Why? "New York has the deepest and most diverse pool of intellectual capital anywhere," says Brian T. Healey, a general partner at the New York

"New York has the deepest and most

ure-capital firm of
rence, Smith &
y. "That's the pri-
y ingredient for
media."

at New York has
than the painters,
s, musicians, and
makers now piling
new media. It's the
headquarters for
communications, adver-
g, media, and pub-
ing conglomerates
as Time Warner,

Hearst, and Bertelsmann—all clus-
t in mid-Manhattan. "This is where
power is," says Stan Winsten, chief
ating officer of R/GA Interactive, a
al-media production house on the
of the garment district. And those
s are thirsting for new-media hits
reverse the slowdown in growth
ed by softening in print and broad-
ing. "Multimedia is one of the oppor-
ties to change that," says Peter B.
ch, president of Simon & Schuster
ractive, one of a dozen new-media
set up by the midtown giants.

NY DOWNTOWN. The proximity of
s of ambitious startups and artists
ep-pocketed corporations in need of
ent makes New York a new-media
a—rivaling such West Coast en-
s as Seattle and Hollywood. Now,
anners and new-media proponents
rying to raise Gotham's profile as a
media center. The New York City
nership, a business and civic group,
eamed up with IBM, Nynex, and
olidated Edison to lease a 35,000-
re-foot building near Wall Street
will serve as a "shared-tenant incu-
" for multimedia and software de-
velopment. It will provide affordable

and cut-rate ser-
ices and equipment to
50 software com-
es. Office and con-
ce facilities will
be available for
le working out of
ome or loft. The
nership hopes the
er will act as a cat-
er for the burgeon-
new-media indus-
and in the process
reinvent the
town economy.

ne new-media boom is clustered in
y neighborhoods such as Tribeca,
n, and the Flatiron district. "Three
s ago, you could count on one hand
people trying to make money off



ADVERTISING

From Curious Pictures,
a spot for Dannon yogurt

by Yee-Ping Wu, a child prodigy pianist
and onetime concert performer turned
software developer.

But the scene has really taken off
in the past two years. In 1993, Robert
Stein moved his multimedia publishing
company, Voyager, from Santa Monica,
Calif., to SoHo. Last year, United Dig-
ital Artists, an outgrowth of the now-
defunct Kodak Center for Creative Im-
ages in Camden, Me., set up shop in
lower Manhattan. The
new-media talent agen-
cy and training center
represents more than
400 local artists and
programmers. Robert
De Niro, who has a
film center in Tribeca,
recently formed an
interactive division, Tri-
beca Interactive. Even
Microsoft Corp. and
Apple Computer Inc.
have dispatched staff-
ers to New York to
work with local developers.

So what are all these new-media en-
trepreneurs up to? Preiss, who founded
his multimedia company in 1992 and
took it public in May,
1994, is cranking out
everything from an
interactive *Seinfeld*
screen-saver for Time
Warner Interactive to
The Ultimate Frank
Lloyd Wright, a CD-ROM
about the architect's
work for Microsoft's
Home line. Preiss's
stock, issued at \$2 a
share, now trades in
the mid-teens.

Music Pen, located in
Union Square, just south of Preiss's
Flatiron digs, is turning out a steady
stream of edutainment titles. They in-
clude *Lenny's Music Tunes*, a series dis-
tributed by Viacom/Paramount, and *The*

this," says Bryan Mc-
Cormick, president of
BAM! Software, a mul-
timedia production com-
pany located on Tri-
beca's Franklin Street.

The downtown scene
began in the mid-'80s
with pioneers such as
Byron Preiss Multi-
media, which created
some of the industry's
first multimedia titles,
and Music Pen, a com-
pany founded in 1987

Magic School Bus Explores the Human
Body, produced for Microsoft.

There's also Take 2 Interactive Soft-
ware, founded a little over two years
ago by Ryan Brandt, the scion of the
New York publishing clan that publish-
es *Interview*, *Antiques*, and *Art in*
America magazines. Brandt, 23, has so
far focused on entertainment—games
such as *Hell*, a CD-ROM thriller starring
Dennis Hopper and Grace Jones. Take 2
has development deals with Apple, Via-
com, and Gametek.

DIGITAL DUET. New York is even giving
Hollywood some competition. R/GA Dig-
ital Studios, a production house that did
special effects for films such as Clint
Eastwood's *In the Line of Fire* and
Woody Allen's *Zelig*, earned a reputation
as the Lucasfilm Ltd. of the East. R/GA's
early bet on digital technology in 1987
has paid off. Like neighbors such as Cu-
rious Pictures, it's now a leading produc-
er of digital ads, including such ground-
breaking work as the Diet Coke spot
that paired Gene Kelly and Paula Abdul

in a digital duet.

Today, R/GA is mak-
ing interactive ads for
Chrysler Corp. and the
U.S. Postal Service to
be tested on Time War-
ner Inc.'s experimental
Orlando cable-TV net-
work. R/GA's Interactive
unit, formed in 1993, is
working on original con-
tent, including two up-
coming CD-ROMs, *Gear*
Heads and *City Golf*,
that are now being pro-

duced for Tribal Media, a joint label
with Philips.

While lots of multimedia program-
ming has been little more than "shovel-
ware"—a term for simply cramming
print or other "old media" content onto
a disk—New York's new-media upstarts
pride themselves on being on the cre-
ative edge. "The sensitivity to content
is a hallmark of New York," says Preiss.

Such creativity has been rewarded
with big contracts from the software
and media giants that have the re-
sources to fund development and pay
for marketing and distribution. But
starting this year, some of New York's
most talented developers—including Mu-
sic Pen, Take 2, and R/GA Interactive—
plan to publish under their own labels,
rather than distributing through Micro-
soft or Time Warner. If they achieve
new-media stardom, they could really
put Silicon Alley on the map.

By Amy Cortese in New York



GAMES

Dennis Hopper stars in
Take 2's CD-ROM *Hell*



EDUTAINMENT

Music Pen's *Magic School Bus*
Explores the Human Body

erse pool of intellectual capital anywhere"

INVESTMENTS

L.T. JUST MIGHT SACK HIS SKEPTICS

The ex-All Pro says his virtual-reality venture is ready to romp

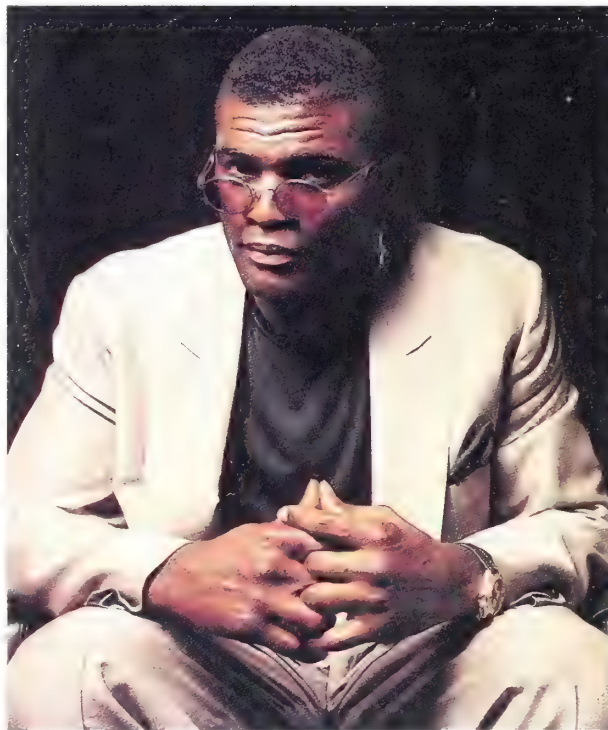
Even before he hung up his cleats a year ago, Lawrence Taylor wanted to be more than a football legend. He wanted to be an entrepreneur. So the New York Giants linebacker formed All-Pro Products Inc. out of his New Jersey home in 1992. Its first game plan: to brew up a sports drink with big-city attitude, something *Hoop Dreams*-ters could chug in the playground after a hot three-on-three. But the Gatorade wannabe, dubbed Metro-Pro, fizzled fast.

With PepsiCo, Coca-Cola Co., and other beverage behemoths pouring megabucks into their own new sports swigs, Taylor and his team soon knew Metro-Pro didn't have a prayer. "Creating a niche for [Metro-Pro] would have taken more time and more money than we had," says All-Pro President and Chief Operating Officer Michael Stone, 54, a former management consultant and one-time COO of New Generation Foods Inc., a snackmaker in Oglesby, Ill. All-Pro lost more than \$500,000 on the drink before bagging Metro-Pro in 1993.

EASY SELL. Then, Taylor met Arden Strasser, 32, a University of Rochester-trained optics whiz and top engineer at Virtual Reality Inc., a Pleasantville (N.Y.) technology company in need of funding. L.T. decided to stake his company's future on an unpaved lane of the I-way, paying \$350,000 plus royalties for a license to use VRI's technology to make a game system. Needing more dough than he was willing to cough up himself, Taylor took All-Pro public in November, 1993, raising \$4.5 million in an initial public offering. Speculators gobbled up 1 million shares overnight in what looked like little more than a gamble on L.T.'s name and the buzz of virtual reality. Offered at 5, the NASDAQ-listed stock quickly soared to 14—though All-Pro had no earnings, no product, and a retired football star at the helm. And it never crashed. On Jan. 17, the stock was trading at 9½, giving All-Pro a market value of \$24.2 million.

Now, after more than two years and \$2 million in development costs, the All-Pro team believes its just unveiled 7th Sense system will justify shareholders'

faith. Retailing for less than \$400, it will hit stores in the Northeast on May 1 and those in the rest of the U.S. in time for Christmas. "Everybody thought we were some kind of scam," concedes Taylor, All-Pro's chairman, CEO, and, with a 40% stake, No. 1 shareholder. But, he



Lawrence Taylor thought he was some kind of scam, now he's in the virtual-reality game.

predicts, "we're going to be a major player" in virtual-reality games.

Designed to be hooked up to an IBM-compatible PC, the 7th Sense system is contained in a lightweight plastic headset that works with a number of games, including—natch—football. Using 7th Sense with a flight-simulator game allows players to "see" out the left side of

the plane when they turn their head left, see the tail of the plane when they look over their shoulder, and see clouds when they look up.

At the time of the IPO, All-Pro appeared less like a public corporation than an extension of Taylor's ego. Married out of a spare room in his Upper Saddle River (N.J.) home, it had just one full-time employee. Its board included two other former pro football players, Paul Davis and George Matlin, who has since resigned. Now headquartered in Tarrytown, N.Y., All-Pro employs 20 people and recently added former Sega Enterprises Ltd. executive, engineer Mark Williams, to its board. In August, it gobbled up New York-based Containair Systems Corp.

a cardboard-box company, for \$700,000 in cash. The subsidiary is expected to generate about \$2.5 million in sales in fiscal 1995, providing much needed cash flow for All-Pro.

BLITZ-WARY. By going after the 36 million at-home PC users instead of creating a TV-based or stand-alone system, All-Pro avoids banging heads with home-entertainment giants such as Nintendo and Sega—for a while. Stone knows those two heavyweights can't be far behind. "I figure we have a window of maybe 18 to 24 months," he says. This year, All-Pro expects to ship at least 50,000 units to such retailers as CompUSA, J&R Computer World, and Nobody Beats the Wiz.

Should 7th Sense flop, skeptics who derided All-Pro's 1993 offering as yet another example of IPO fever will probably be crying. And while Taylor insists that he would move forward and find another product, All-Pro's ability to raise money would be diminished. But if 7th Sense becomes something more than a virtual success, L.T.'s post-NFL earnings could make the millions he's gambling heads to the turf seem like chump change.

By Keith Dunnivant in Tarrytown, N.Y., and Carl Desens in New York

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PLUMPER PROFITS, SKIMPIER PAYCHECKS

But economists say labor will benefit—eventually

It seems the best of all worlds. The U.S. economy is hitting on all cylinders: strong growth, low inflation, and a steady flow of new jobs. And U.S. companies, on the ropes in the mid-1980s, are world-class players again.

This prosperity, however, conceals a dramatic shift in who is benefiting from the revival of Corporate America. A new BUSINESS WEEK analysis of national income generated by the corporate sector—labor compensation, profits, and interest payments—shows that workers are getting the short end of the stick. Over the last two years, the share going to labor has dropped sharply. Only 81% of corporate income now goes to wages, salaries, and benefits, the lowest level since 1969. And wages and salaries alone are now less than 67% of income, a post-war low, as downsizing, job cuts, and wage restraint continue to dominate business strategies.

MAJOR IMPACT. These numbers confirm what many Americans feel in their bones: Workers have not yet seen big gains from rising productivity and the strong economy. Instead, the major impact of the good news has shown up in profits. Operating profits, as measured by the government, have risen to over 15% percent of national income in the corporate sector, their highest level in almost 20 years. And with fourth-quarter corporate earnings expected to be strong,

that figure could rise even higher.

But while it may be frustrating to workers to see real wages stagnate, even as the economy prospers and profits soar, history and economic theory suggest that they may see benefits a little further down the road. Since the days of Adam Smith, economists have studied how the economic pie is split between payments to labor—wages, salaries, and benefits—and returns to capital—profits and interest on debt. This division influences everything from the distribution of income to the economy's potential rate of growth. Periods with a high profit share have typically also enjoyed rising productivity, high levels of investment, low inflation, and eventually strong wage growth. "What high returns on capital give you is the possibility that you can grow faster," says Richard D. Rippe, chief economist at Prudential Securities Inc. Adds Fred Moseley, an economist at Mount Holyoke College: "Profitability is the most important determinant of the health of the economy."

Certainly that's been true for most of the 20th century in the U.S. In the 1920s, for example, high profitability and a small labor share was accompanied by rising living standards. And the last time labor had as small a share as it does today was the 1960s, which is remembered as a prosperous period for most everyone. Strong profitability helped fund high



investment, keeping productivity robust and inflation low. And the strong growth of the overall economy meant that real wages could grow fast enough to keep workers happy.

Like an earthquake fault line, the labor-capital split may hardly change decades. But when the balance shifts, the move is quick and dramatic. The beginning of the 1970s, for example, saw a substantial increase in the share of income going to labor that persisted over the next two decades, as workers—especially ones in strong unions—were able to push up real wages even as productivity growth slowed.

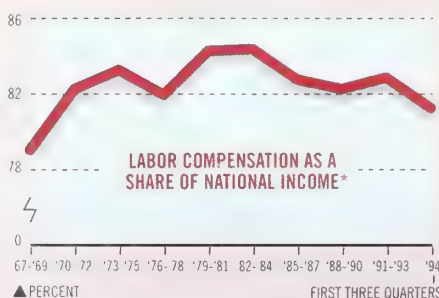
But that increase turned out to be a pyrrhic victory for labor. While workers may have benefited in the short

A Startling Shift in Income Shares

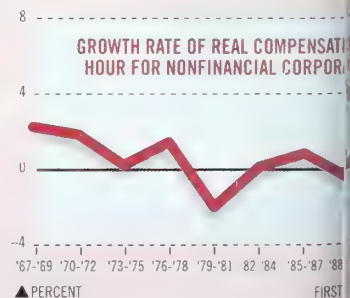
*IN THE CORPORATE SECTOR

DATA: COMMERCE DEPT., LABOR DEPT., BUSINESS WEEK

WORKERS GET A SMALLER SHARE...



...AND REAL WAGES STAGNATE...





With downsizing the dominant strategy, wages, salaries, and benefits now account for only 81% of the share of national income generated by the corporate sector—the lowest level since 1969

a bigger share, the eventual re- of lower profits were slower h and less investment. In addi- s Moseley notes, the double-digit on of that decade was in part the of companies trying to alleviate profit squeeze by raising prices—a gy that did not work.

w the U.S. may be in the midst of er tectonic change in the split be- labor and capital. Corporations been able to boost productivity, a combination of restructuring, izing, and investment in new tech- . And while the unemployment as fallen, wage growth has been own by international competition, echnology—which needs a lot less —and the impotence of labor

unions. In the 1960s, real compensation per hour in nonfinancial corporations rose at an average rate of 2.1%. By contrast, real compensation per hour fell by 0.3% in the first three quarters of 1994 compared with a year earlier.

Indeed, in recent years, some of America's largest companies have dramatically pared down the share of revenues going to workers by boosting productivity, cutting jobs, holding down wages, and outsourcing. For example, General Motors Corp. spent 26% of its revenues on wages, salaries, and benefits in 1989. But by 1993, the percentage of revenues going to labor was only 22%.

With profits' share of corporate income rising again, today's economy is beginning to look a lot more like that of

the low-inflation 1960s. Corporate productivity growth is strong, clocking in at 3% in 1994, the highest in two decades. Companies are pouring hundreds of billions into new equipment. And with profits high, they can hold off on price increases, keeping inflation dormant.

Moreover, the rising capital share is good news for the stock market, which, not surprisingly, has historically benefited when profits took a bigger bite of the pie. Indeed, the market is far more responsive to the profit share than it is to the overall growth of the economy. **MARKET MOVER?** Certainly, the shift from wages to profits is the major reason the stock market hasn't taken a deep dive in light of the massive interest rate increases by the Federal Reserve. Rippe calculates that the rate of return on capital, adjusted for inflation, has reached about 6.5%, a 25-year high, which may propel the markets even higher. "I don't believe that the conventional wisdom in business has fully recognized" how much corporate profitability has increased in recent years, says Rippe.

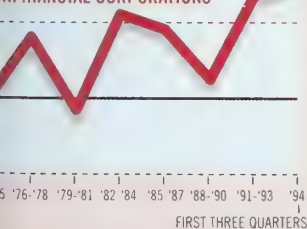
The rising profit share also changes the nature of the income-distribution debate. In recent years, both economists and policymakers have concentrated their attention on the widening inequality of wages, looking for ways to narrow the difference. But this leaves out the widening gap between Americans with capital income and those without. Wages are far less important than they used to be as a source of income. Americans now get only 57% of their personal income from wages and salaries, a post-war low. Instead, dividends and self-employment income have become progressively more important. Moreover, notes economist Louis A. Ferleger of the University of Massachusetts at Boston, wage income will shrink even further if the Republicans carry through on their plans to downsize government, since the public sector now accounts for a full 20% of all labor compensation.

With the division of income shifting in favor of capital, when does the payoff for workers come? It took almost a decade for the real wages of workers to adjust to the productivity slowdown of the 1970s. That means it could take some time before wages respond to the improved economic conditions in the 1990s. "The economy is growing, but a large portion of the public are very upset because their real wages aren't going up," says Robert Eisner, an economist at Northwestern University and a former president of the American Economic Assn. Workers will eventually gain if higher profits lead to more investment and more jobs, adds Moseley, "but it hurts a lot."

By Michael J. Mandel in New York

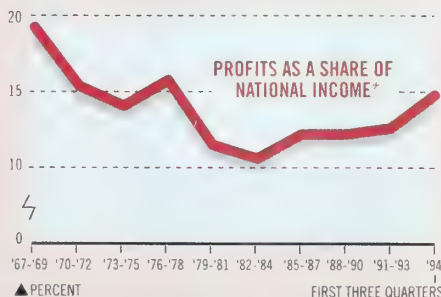
AS PRODUCTIVITY RISES...

PRODUCTIVITY GROWTH RATE FOR NONFINANCIAL CORPORATIONS



...AND PROFITS SURGE

PROFITS AS A SHARE OF NATIONAL INCOME*



Business Week and The Association of American Chambers of Commerce in Latin America (AACCLA) present

The BUSINESS FUTURE of the AMERICAS

Strategies for an Integrating Hemisphere

by James R. Whelan

They came to the land that turned the promise of the free market into the reality of plenitude. The land is Chile. And "they" are the 150-plus business and government leaders from all parts of the hemisphere who gathered in Santiago for the *Business Week/Association of American Chambers of Commerce in Latin America (AACCLA)* "Business Future of the Americas" conference.

TRADE, TRADE, TRADE

Trade was a key theme. AACCLA President David E. Ivy urged that "the United States and nations of the region continue to work toward lowering trade barriers. It is important to begin adding nations that have opened their markets, and there is no better candidate than Chile."

Chilean Finance Minister, Eduardo Aninat reminded the conference that trade liberalization is more than lower tariffs. "Economic integration," said Aninat, "means legislation setting the ground rules for foreign investment, it means fixing arbitration standards, it means agreeing on competitive frameworks. It means less rhetoric, more action, and it means converting economists' conclusions into implemented national policy."

The new U.S. Ambassador to Chile, Gabriel Guerra Mondragón, underscored the point. "Our world is going global, and to go global means overcoming past habits of focusing on differences while overlooking similarities." As an example of "going global," he observed that the architects of the widely lionized "Chilean model" are now giving their how-to advice to governments around the world.

TIN AMERICAN MULTINATIONALS

Meanwhile, under new free-trade minded Latin American governments like Chile's, scores of Latin American firms are moving from domestically focused strategies to become global players.



"The United States and nations of the region continue to work toward lowering trade barriers. It is important to begin adding nations that have opened their markets, and there is no better candidate than Chile."

David E. Ivy, President,
The Association of
American Chambers of
Commerce in Latin
America (AACCLA)

Alan Clutterbuck, director of the Argentine footwear and textile firm Alpargatas, is focusing on the emerging Mercosur free-trade bloc and building joint ventures and alliances with the likes of U.S.-based Nike.

Andrés Navarro, President of Sonda, the international information systems design company, has used newly opened regional markets to take the company from zero to \$140 million in sales and 1,300 employees in just 14 years.

U.S. COMPANIES IN LATIN AMERICA

As Latin American firms are breaking out of previously locked-up national markets, U.S. firms are breaking in. Across the board they are recognizing the importance of being there. "Long-distance management does not work," said Han Eben, President, Andean Region/Chile, The Gillette Company, noting that more than 30 international companies now have regional headquarters in Santiago.

BellSouth Latin America President Roberto Peón, offered his recipe for success. "Use common sense at all times; think big. Dig in — make no exit plan. And maintain a sharp focus on what you do best." BellSouth Latin America decided to focus on cellular and wireless. From ground zero five years ago, the company now serves 312,000 customers.

But Peón acknowledged that it can be difficult for an upstart subsidiary in a large company like \$16 billion BellSouth to get the attention and resources requisite for



economic integration
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success. "Quite frankly there was a lot of skepticism. But as we became successful, we were viewed by upper management as an example for other operations."

For Kodak, surviving the protectionist era in Latin America meant 11 separate country operations. Charles Griffin, president of the Kodak Group of Mexico, said all of that changed with the opening of markets. "We streamlined down to five 'boundaryless' companies, and, taking advantage of trade openings, we created centralized distribution, slashing delivery time and inventories."

Operating internationally was a birthright of the American International Group, spawned in China and now a prime example of an American company aware of and responsive to the world outside the

As President of the company's Life Management on for Latin America, Alexander Fernández supervises fices. Fernández noted that when he headed operations in years ago, there were 12 competitors. Now there are 25. he added, "that is not as bad as it sounds. The Chilean much larger now than it was then."

Successes have a tendency to grow rapidly in today's Latin American business environment. Tim Browne, Director of International Marketing for Lotus Development Corporation, his own firm: "Our Latin American divisions used to t through our European operations. But with the rapidly ring communications infrastructure in Latin America, ow have our two Latin American divisions as well as a ng community of Latin American Business Partners all ected directly to each other, and to our orate Headquarters in the USA. These ections using Lotus Notes have created an ization for us that can respond to the mer needs, no matter where they are located. matter of seconds rather than hours or days. has allowed us to move our operations hroughout all of Latin America quickly and ently." The company is organized into small sales teams supported by more than 20 Latin American "business partners" and ectronic network that offers each team full ay access to more than 7,000 business ers worldwide.

W LATIN AMERICA IS VATIZING SOCIAL SECURITY

A. Viada, Regional Head/Latin America
andard & Poor's Ratings Group chaired a

session on the Chilean capital market, where discussion focused on Chile's highly successful voluntary private pension funds. The funds have paid-in capital equal to more than half the country's gross national product, and Viada credits them with the central role in developing Chile's domestic capital markets. "They are the most profound and revolutionary development in the Chilean economy," said Viada.

The father of Chile's private pensions system, Jose Piñera, said the pensions have created an enormous pool for re-investment, averaging a 13% rate of return since their 1981 debut. Since then, fund money has financed two of three new houses built in Chile while one-third of all shares in the stock market are fund-held.

"The Chilean model has been copied enthusiastically," said Piñera, "so far this has occurred in Peru, Argentina, and Colombia. Bolivia, Ecuador, and El Salvador are likely to follow soon. And it is only a matter of time until Brazil goes down the same road."

SOUTHERN SUCCESS STORIES

U.S. Deputy Assistant Secretary of State Arturo Valenzuela sketched the dimensions of the Latin American opportunity: "By decade's end the combined gross domestic product of Latin America will be about \$2.5 trillion, roughly equal to Japan's." Mexico's, he noted, is already larger than that of South Korea. Furthermore, annual regional growth is expected to average 5% over the next decade — twice that of the European Community.

Summing up, David Hirschmann, Executive Vice-President of AACCLA, said: "Senior decision makers from around the hemisphere and strategies businesses are embracing in a region now dominated by expanding, integrating economies. This conference has become for Latin America what the annual Davos economic conference is for Europe — the place where new business trends are identified and new business relationships are launched."

James R. Whelan, a visiting professor at the University of Chile's Institute of Political Science, is a foreign correspondent in Latin America and a visiting professor at the University of Chile's Institute of Political Science.



"Latin America has enormous growth potential in the communications industry. Taking advantage of this has allowed Lotus to move through Latin America quickly and efficiently."

Tim Browne, Director of International Marketing, Lotus Development Corporation



"Use common sense at all times; think big. Dig in — make no exit plan. And maintain a sharp focus on what you do best."

Roberto Peón, President, BellSouth Latin America

EDITED BY AMY DUNKIN

MAKING YOUR LONG-DISTANCE DOLLAR GO THE DISTANCE

Bill Adler Jr. proudly admits he has no loyalty when it comes to long-distance calling. Last month, the Washington (D.C.) book agent switched his three home lines from AT&T to MCI so he could earn American Airlines frequent-flier miles. Less than a month later, he changed one line to Long Distance Wholesale Club, which offered seemingly low rates plus 50% off his next bill. But once he gets the half-off bonus, he is poised to switch again: "I'll go with whoever is offering me the best deal."

There will be plenty to

you spend just \$10 a month. That means a \$50 monthly bill becomes \$37.50. The discount increases to 30% when your monthly tab hits \$75. And you get 50% off when you call other MCI customers in your designated calling circle. If you signed up for the old Friends & Family program, you have to ask to be switched to the new one. The old

If your calling falls into a distinct pattern, check out more tailored plans. AT&T Evening Plus is aimed at those who make a lot of calls on weekends or after 5 p.m. on weekdays. It charges 12¢ per minute for one hour's worth of calls and 10¢ a minute beyond that

ized" phone rates. Like a first-class stamp, there is a flat rate—on a per-minute basis—regardless of the distance of the call. LCI is particularly attractive for customers who make hundreds of dollars' worth of calls a month because it bills in six-second increments. While most companies would bill you four minutes for a call that lasts three minutes, or two seconds, LCI would charge for three minutes, six seconds and so on.

You almost always pay a premium for the simpler system, however. With Sprint Sense, you pay a hefty flat rate of 22¢ a minute during



choose from. AT&T started a rate war last year, and MCI and Sprint struck back this month. But figuring out which of these companies—or their smaller rivals—offers the best discount scheme for you requires a hard look at where, when, and how much you call long distance.

TAILORED TRACK. Most plans base their rates on time of day, distance, and volume of calls. If you typically have a monthly bill of less than \$75 and a scattershot pattern of calls—over both long and short distances and at varying times of day—MCI's new Friends & Family plan is probably your best bet. MCI offers a 25% discount after

plan provides 20% discounts and 40% off for dialing others in your calling circle.

The new MCI program usually beats AT&T's True USA plan. While AT&T, like MCI, begins its discount at the \$10 calling level, it offers only 10% off at that point. And the discount only rises to 20% after you spend \$25. The two programs begin to reach parity when the monthly bill hits \$75, when AT&T gives you the same 30% off as MCI. But MCI remains a better deal because the basic rates on which its discounts are calculated are slightly lower.

hour. Those whose calls aren't limited to off-peak hours but are targeted to a particular area code might consider a plan like AT&T's Select Saver. It charges a competitive 20¢ a minute for weekday calls during the day. There is a drawback to Select Saver and Evening Plus, however. If you don't call within the right time periods or to the right location, you get zinged with much higher rates.

If you make a lot of calls over very long distances—say, from New York to California—two plans heavily promoted by Sprint and LCI International may be for you. These companies offer "postal-

the day, though the 10¢ rate for evenings and weekends is competitive. Once again there's a catch: While Sprint's day rates extend to 7 p.m., others end the day at 5 p.m. So those who hope to get the low evening rate at 6 p.m. won't find the scheme a bargain.

The plans also have initial come-ons. Sprint Sense throws in 100 free minutes of talk time to sign up. And in April, the company, which is aligned with cable giants TCI, Cox Enterprises, and Comcast, is expected to offer several months of free cable programming to new customers.

Not to be outdone, MCI will cut your bill in half for six months if you sign up for tele-

PHONING

Friends & Family.
last year, AT&T
been sending out
\$75 checks to
age people to
. Endorsing the
means you have
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True Rewards
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The points—earned if
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ivalent amount of fre-
-flier miles on USAir,
d, or Delta. MCI offers
at the same rate on

Phone Deals: Cutting Through The Static

	PLAN	COMMENT
AT&T TRUE USA	10% off a bill of \$10 to \$24.99 a month; 20% off \$25 to \$74.99; 30% off \$75 or more.	People who make fewer than \$75 worth of calls in a month can get a better deal elsewhere.
MCI "NEW" FRIENDS & FAMILY	25% off \$10 to \$74.99; 30% off \$75 or more; 50% off calls made to designated MCI customers.	MCI will slash your bills in half for six months just to sign up. The plan edges out True USA, especially at lower calling volumes.
SPRINT SENSE	22¢ a minute 7 a.m. to 7 p.m. Mon. to Fri.; 10¢ weekends and 7 p.m. to 7 a.m. weekdays; \$3 a month beginning Apr. 1 for low-volume callers.	The company makes a big deal out of its simple flat rates. But some customers could pay more, since Sprint keeps its highest "day" rates in place until 7 p.m.

Northwest, American, and Continental. Sprint has alliances with TWA, Alaska Airlines, and America West. But its new reward plan also gives certificates for discounts on any airline, cruise, or car rental—without blackout dates.

You can use reward points for free calling if you choose. AT&T gives roughly a minute and a half of extra time for each dollar spent with all of its plans. If you spend \$50 a month with Sprint, you could qualify in 10 months for \$25

of free calling. Some plans even give you money back. AT&T offers a cash rebate of 5¢ on the dollar. If you spend \$100 a month you could get a \$60 check at the end of the year.

Freebies shouldn't be the decisive factor in choosing a long-distance carrier. The higher bills you would incur by picking an unsuitable plan could well offset the inducements. But from time to time, you can make out by jumping ship. You've got nothing to lose since your new carrier will pay your local phone company the charge for changing long-distance companies. And once the enticements for new customers are gone, you can move on. Any way you look at it, it's a caller's market. *Mark Lewyn*

HART MONEY

HERE'S THE CHEAPEST BANKING?

the past few
rs, low-yielding
ney-market funds
e been a place to
n cash while you move
and out of real invest-
ts. But with stock and
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y and money funds
ling an average of
%, the latter once again
s an investment option
s own right. Investors
taking notice. The week
ed Jan. 13 marked a
high of \$528 billion in
ble money-fund as-
—up from \$509 billion
ec. 31, according to
Donoghue's *Money*
d Report.
you plan to stay in a

money fund for a while, though, pay close attention to the expense ratio. Since money funds generally invest in similar, low-risk securities, the fee is a major determinant of differences in yield. Many money funds are loaded with freebies, such as check-writing and switching among funds. But if you don't need such services and can afford a hefty initial investment, you may be better off in a fund that discourages small transactions with nuisance fees and high check minimums and then compensates with lower expenses and fatter yields.

For example, the \$50,000 minimum Vanguard Admiral U.S. Treasury Money Market Fund charges only 0.15% in expenses and yields 5.36%. The average government-only money

fund yields 5.07%. Fidelity Spartan Money Market Fund, paying 5.52%, has a \$20,000 minimum and a 0.44% fee. The average money fund charges 0.57%. **LONG VIEW.** True, plenty of money funds boast lower expenses than the high-minimum funds. That's because nearly 60% of all money funds currently waive some or all of their expenses to boost their yields, a practice that became common as yields fell to 3%. But there's

always the danger that these fees will be phased back in, causing the yield to fall.

If you are enticed by the yield on a fund that is not charging a fee, check to see how long the waiver will be in effect. Strong Money Market Fund—the top yielder at 6.23%—guarantees to forgo all fees through June, 1995. Flex-Funds Money Market Fund promises to waive part of the management fee in order to stay in the top 10% of money funds. Vanguard disapproves of fee waivers on the grounds that they mislead investors about yield. Instead, its regular money fund holds expenses to 0.32%. So there are plenty of low-fee goodies even if you don't have \$50,000 to invest. *Amey Stone*

Money Funds For Investing

FUND	CURRENT YIELD*	MINIMUM	EXPENSE RATIO
DREYFUS BASIC Money Market	5.86%	\$25,000	0.24%
FIDELITY SPARTAN Money Market	5.52	20,000	0.44
T. ROWE PRICE SUMMIT Cash Reserves	5.65	25,000	0.45
VANGUARD ADMIRAL U.S. Treasury Money Market	5.36	50,000	0.15

*Seven-day yield

DATA COMPANIES

THREE FOR THE ROAD-OR TRAIL

They're rugged, they're roomy, and they're roaring off showroom floors.

Sport-utility vehicles are the hottest segment of the auto market today, so makers keep introducing new models and upgrading their old ones. The all-new Land Rover Discovery and Chevy Blazer and the heavily revamped Ford Explorer are three of the latest in the so-called compact segment.

The Discovery is supposedly the *veddy* British auto maker's family model, an oblique reference to its dual air bags and price tag of \$29,525 (all prices include destination charges). While still rather high among this trio, that's not quite as stratospheric as the \$53,125 for the

above the front and rear seats—they provide more light and visibility for passengers on the optional jump seats in the cargo area. In theory, those seats allow room for two more people in back. In reality, Discovery's claims of spaciousness apply only to headroom. There is so little knee- and legroom in the jump seats that fitting seven people means you won't have room for carrying any stuff.

Also on the negative side, this vehicle emits a whine from the full-time all-wheel drive, has a high step-in height, and contains nothing solid to completely close off the sunroofs, only dark-mesh shades to keep the sun out. You wonder if they'll do the trick in Arizona.

Yet if four or fewer folks climb in, they'll find a well-appointed, luxurious interior for a vehicle built to handle serious off-roading. The high ride height is misleading: Although the Discovery offers plenty of ground clearance, the center of gravity is still low enough for stability. And there's considerable oomph from

the 182-horsepower V-8 engine. It is the most powerful among this trio of sport-utes, but then, the Discovery needs more power because it is the heaviest at 4,379 pounds, vs. Explorer's 4,189 and Blazer's 4,020. Notice, though, that there is no red line on the tachometer warning you to shift now or else: This engine is ready to rev in any gear.

In contrast, the rough-revving engine is one of the few disappointments in the Ford Explorer. The V-6, carried over from the previous-generation Explorer, delivers 160 horses. That's enough to do the job but well below the other two vehicles' muscle. The optional running board is almost a necessity, given the steep climb into the

el is one of the few weak points in the new Chevy Blazer, which is virtually identical to its sister model, the GMC Jimmy. Most of the controls are laid out well, but you have to reach behind the gearshift lever to toggle between AM and radio bands.

Still, Chevy's all-new sport-ute is vastly superior to its predecessor. The step-in height is quite low, an obvious and welcome nod to the large numbers of women buying these vehicles. Wind and road noise have been reduced substantially, and the resulting quiet at highway speeds is fitting, since the Blazer has the best on-pavement ride of this trio. The Blazer is competitively priced at a base \$22,763 for four doors and four-wheel drive.

What don't you get that money? The Blazer has only a driver's-side air bag. Moreover, the four-wheel drive system is trickier to engage than those of its rivals, and the four-wheel lock brakes are startling in their loudness. After all, ve-



FORD EXPLORER

\$22,805* 4.0 liter V-6/160 hp
Two front air bags

*Price is for the base four-door, four-wheel-drive version with destination charges. Explorer and Blazer also come in less expensive two-wheel-drive models

Range Rover County LWB.

Other features are different, also. The excessive body roll associated with most Land Rovers is gone—good news for those prone to seasickness. Above the far rear windows are extra windows running along the crease where the roof meets side panels, together with the optional dual sunroofs—one each



CHEVROLET BLAZER

\$22,763* 4.3 liter V-6/195 hp
Driver's-side air bag only

seats. The price for the base four-door, four-wheel-drive version is \$22,805. (Both Explorer and Blazer offer less pricey two-door, two-wheel-drive models.)

INTERIOR MOTIVE. Elsewhere, the Explorer shows numerous signs of improvement and refinement. The Explorer has a new front suspension and new power steering, the better to handle on-road driving. Also, the interior has been redesigned, giving it a vastly improved instrument panel and controls—and dual air bags. Check out the tissue dispenser between the front seats. A simple rotary knob on the dash switches you from two-wheel drive to the excellent four-wheel-drive system and on to four-wheel low, used for even bumpier off-roading. There's a reason the Explorer has been a best-seller, and most of it is in the interior.

The boxy instrument pan-



LAND ROVER DISCOVERY

\$29,525 3.9 liter V-8/182 hp
Two front air bags

needs more sensory overload when panic braking? Nonetheless, the Chevy Blazer offers quite a lot for the money in a segment where prices are getting steeper the hills that four-wheel drive can conquer. *Jim Tre*

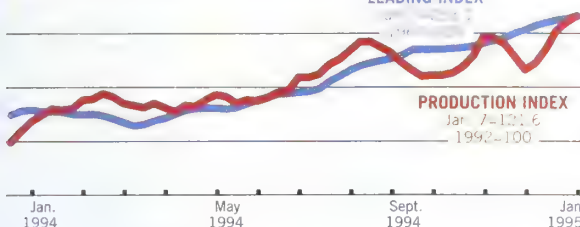
Business Week Index

PRODUCTION AND LEADING INDEXES

Change from last week: 0.5%
Change from last year: 7.6%

Change from last week: 0.2%
Change from last year: 7.5%

LEADING INDEX



The production index increased during the week ended Jan. 7. Seasonally adjusted output of crude-oil refining and rail-freight traffic led the gain. Before calculation of the four-week moving average, the index rose to 121, from 120.8.

The leading index also advanced during the latest week paced by faster growth rates for materials prices and real estate loans. The unaveraged index increased to 254.6, from 253 in the previous week.

Production index copyright 1994 by McGraw-Hill Inc.

BW leading index copyright 1994 by CIBC

LEADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (1/13) S&P 500	462.36	460.21	-2.5
CORPORATE BOND YIELD, Aaa (1/13)	8.46%	8.51%	23.1
INDUSTRIAL MATERIALS PRICES (1/13)	114.3	113.3r	NA*
BUSINESS FAILURES (1/6)	NA	278	NA
REAL ESTATE LOANS (1/4) billions	\$459.8	\$456.6	9.0
MONEY SUPPLY, M2 (1/2) billions	\$3,571.1	\$3,570.6r	0.9
INITIAL CLAIMS, UNEMPLOYMENT (12/31) thous.	338	321	-4.8

Sources: Center for International Business Cycle Research (CIBC), Standard & Poor's, Moody's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures of large companies), Federal Reserve, Labor Dept. CIBC seasonally adjusts data on business failures and real estate loans. *Historical data available from CIBC.

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
FEDERAL FUNDS (1/17)	5.69%	5.44%	3.13%
COMMERCIAL PAPER (1/17) 3-month	6.09	6.18	3.18
CERTIFICATES OF DEPOSIT (1/18) 3-month	6.22	6.18	3.12
FIXED MORTGAGE (1/13) 30-year	9.35	9.39	7.09
ADJUSTABLE MORTGAGE (1/13) one-year	6.88	6.85	4.25
PRIME (1/18)	8.50	8.50	6.00

Sources: Federal Reserve, HSH Associates, Reuters Holdings PLC

Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

FEDERAL BUDGET

Tuesday, Jan. 24 ▶ The U. S. Treasury will report a deficit of \$4 billion for December, says the median forecast of economists surveyed by MMS International, division of McGraw-Hill Inc. Quarterly income tax payments are due in December, the government had to send out Jan. Social Security payments early because Jan. 1 was the New Year's holiday. In December, 1993, Washington chalked up a deficit of \$7.7 billion. The nonpartisan Congressional Budget Office recently projected that the federal deficit for fiscal 1995, which began in October, will total \$76 billion. In 1994, the government's deficit was \$203.4 billion.

EXISTING HOME SALES

Wednesday, Jan. 25, 9:45 a.m. ▶ Sales of existing homes likely fell to an annual rate of 3.76 million in December. If so, that would be the fourth drop in five months. In November, resales fell 2.6%, to 3.81 million.

DURABLE GOODS ORDERS

Thursday, Jan. 26, 8:30 a.m. ▶ The MMS median forecast is that new orders for durable goods in December were little changed from their November level. In that month, increased bookings for aircraft and motor vehicles led to a solid 3.4% gain in total new orders. Unfilled orders probably dropped last month, after rising a small 0.6% in November.

GROSS DOMESTIC PRODUCT

Friday, Jan. 27, 8:30 a.m. ▶ Real GDP likely grew at an annual rate of 4.3% in the fourth quarter of 1994, says the MMS report. Thanks to strong job and income growth, consumers continued to increase their spending at a pace exceeding 4%. Business investment in equipment and non-residential construction also probably added to growth at yearend. The fourth quarter would mark the third straight quarter that the U. S. economy grew by 4% or more. In the third period, real GDP expanded at a pace of 4%. Inflation, as measured by the GDP price deflator, is expected at an annual rate of 2.2% in the fourth quarter, about the same rate as in the third quarter.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (1/14) thous. of net tons	2,035	1,985#	7.6
AUTOS (1/14) units	126,386	109,340r#	-7.5
TRUCKS (1/14) units	101,237	84,941r#	-8.7
ELECTRIC POWER (1/14) millions of kilowatt-hrs	NA	63,158#	NA
CRUDE-OIL REFINING (1/14) thous. of bbl./day	13,847	14,336#	2.7
COAL (1/7) thous. of net tons	17,702#	16,047	-3.3
PAPERBOARD (1/7) thous. of tons	NA	NA	NA
PAPER (1/7) thous. of tons	NA	NA	NA
LUMBER (1/7) millions of ft.	364.5#	308.9	-23.2
RAIL FREIGHT (1/7) billions of ton-miles	19.5#	19.3	-5.3

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA¹, SFPA², Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (1/18) \$/troy oz.	382.600	375.600	-2.2
STEEL SCRAP (1/17) #1 heavy, \$/ton	147.00	144.00	5.4
COPPER (1/14) \$/lb.	144.0	139.9	67.5
ALUMINUM (1/14) \$/lb.	98.0	96.5	75.0
COTTON (1/14) strict low middling 1-1/16 in., \$/lb.	87.34	86.12	35.0
OIL (1/17) \$/bbl.	18.35	17.42	20.7

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (1/18)	99.52	99.88	110.60
GERMAN MARK (1/18)	1.53	1.54	1.74
BRITISH POUND (1/18)	1.57	1.56	1.50
FRENCH FRANC (1/18)	5.29	5.30	5.92
ITALIAN LIRA (1/18)	1616.5	1624.0	1696.8
CANADIAN DOLLAR (1/18)	1.42	1.41	1.31
MEXICAN PESO (1/18) ³	5.300	5.725	3.103

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

Whaddya Say To
A Guy Who's Had
The Same Job
For 50 Years,
Has Never Called
In Sick Or
Showed Up Late,
Never Taken A
Vacation Or A
Holiday, Never
Asked For A
Raise Or Griped
About His Bonus
And, Believe It Or
Not, Has No
Plans For
Retirement?



Thanks.

...you can prevent forest fires

Index to Companies

This index gives the starting page for a story or feature with a significant reference to a company. Most subsidiaries are indexed under their own names. Companies listed only in tables are not included.

A

Acer America 38
ACTV 80
Advanced Micro Devices 38
Alaska Airlines 90
Alda Technologies 20
All-Pro Products 84
American Airlines 90
American General Hospitality 50
American International Group 48
American Paging 75
American Research Group 45
America Online 10
America West 90
Apple Computer 38, 39, 62, 81, 82
ARS 38
Art Guard International 75
AT&T 48, 90

B

Bain Capital 8
BAM Software 82
Bankers Trust 76
Bank of Japan 40
Barrow Street Research 80
Bates Worldwide 42
Bell Atlantic 16
Bell Laboratories 62
Bertelsmann 82
Borland International 42
Bose 81
Boston Federal Savings Bank 78
Bridgestone/Firestone 30
British Telecommunications 48
Byron Preiss Multimedia 82

C

Cadbury Schweppes 80
Campbell Soup 86
Canara Bank 48
Canon 62
Capital Growth Management 60
Casio 62
Chase Manhattan 76
Chrysler 82
Ciociola Advertising 39
Citibank 76
C.J. Lawrence 60
CNN 80
Coca-Cola 42, 48, 84
Comcast 90
Compaq Computer 6, 38, 39
CompUSA 84
Conoco 50
Consolidated Edison 82
Containair Systems 84
Continental Airlines 90
Continental Bank 76
Cooper Tire & Rubber 30
Cox Enterprises 90
Cramer Rosenthal McGwynn 60
CS First Boston 48
CSC Index Consulting Group 16
Curious Pictures 82
Cyril 38

D

DDB Needham Worldwide 39
Delta Air Lines 90
Detroit Tigers 57
Digital Equipment 39, 62
Display Technologies 40
Domino's Pizza 57
Don Olson Tire & Auto Centers 30
Donaldson, Lufkin & Jenrette 60, 80
Dr Pepper/Seven-Up 80

E

Eastman Kodak 62, 68
Enron 48
ExerHealth 8
Express America Mortgage 79

F

Federal Express 16
Fidelity 91
Fidelity Management 80
Fidelity Spartan Money Market Fund 91
First Fidelity Bancorp 42
First Union 76
Flex-Funds Money Market Fund 91
Ford 48, 92
Ford España 46
Four Seasons 16
Frank Russell 35
Frito-Lay 16
Fuji Bank 76
Fuji Photo Film 62
Fujitsu 62

G

Gametek 82
Gartner Group 81
Gazprom 50
GE 48, 86
Ganearale de Banque 46
Gibson Greetings 76
Globalink 20
GM 42, 86, 92
Goldman Sachs 60
Goodyear Tire & Rubber 30
Greenwich Associates 35

H

H&R Block 10
Hanna-Barbera Cartoons 75
Hearst 82
Hewlett-Packard 16, 48, 62, 81
Hoffmann-La Roche 72
Hosiden 40

I

IBC/Donoghue 91
IBM 6, 38, 39, 40, 42, 81, 82
Icon 8
Intel 16, 38
International Data 6
Interstate/Johnson Lane 80

J

J&R Computer World 38, 84
James Capel 46
Jardine Fleming Securities 40

John Alden Life Insurance 81
Josephthal Lyon & Ross 80

K

Kellogg 48
Ketchum Communications 39
Kirin Brewery 40
Kmart 42

L

Lawrence, Smith & Horey 82
LCI 90
Lehman Brothers 35, 46
Little Caesar Enterprises 57
Lucasfilm 82
Lukoil 50

M

Matsushita Electric Industrial 40
McDonald's 86
McDonnell Douglas 35
McGraw-Hill 93
MCI 90
Medco Containment Services 62
Medtronic 72
Merck 72
Merrill Lynch 42, 57
Microsoft 20, 39, 62, 82
Mission Energy 48
MMS International 93
Morgan Stanley 80
Motorola 38, 62, 81
MTV 39
Music Pen 82

N

NationsBank 42
NeoVision 72
Nestlé 48
Neuberger & Berman 60
New Generation Foods 84
New York Giants 84
NexGen 38
Nexus Telecommunication Systems 75
Nikon 62
Nintendo 42, 84
Nobody Beats the Wiz 84
Nomura Securities 35
North Carolina Steel 60
Northwest Airlines 90
Nucor 80
Nynex 82

O

Ogilvy & Mather Worldwide 39
Omron 40
Oppenheimer 60

P

Papa John's 57
Pension Consulting Alliance 35
PepsiCo 84
Peugeot 46
Philips Electronics 82
Pilgrim Group 79
Pilgrim MagnaCap Fund 79
Pilgrim Prime Rate Trust 79
Pilgrim Regional Bankshares 79
Pizza Hut 57

Procter & Gamble 76
Prudential Securities 6, 62, 86

Q

Quaker Oats 42
Quarterdeck Investments 60

R

Revlon 81
R/GA Interactive 82
Robertson Stephens 38
Rover 92
Royal Crown Cola 80

S

Saatchi & Saatchi 42
Saint-Gobain 46
Salomon Brothers 57
Samsung Electronics 42, 75
Sega 84
S. G. Warburg 42
Silicon Graphics 81
Simon & Schuster 82
Smith Barney 91
Sony 62, 82
Sprint 90
State Street Boston 35
Sterling Drug 62
Strong Money Market Fund 91
Sun Microsystems 62, 8
Swiss Bank 46, 76

T

Take 2 Interactive Software 82
Tata Group 48
Tele-Communications 80, 90
Teledyne 60
Thinking Machines 81
Time Warner 82
Toshiba 40
Triarc 80
Tribal Media 82
Tribeca Interactive 82
Turner Broadcasting System 80
TWA 90
Tyson Foods 42

U

United Airlines 90
United Digital Artists 82
USAir 90
U S West 48

V

Vanguard Admiral U.S. Treasury Money Market Fund 91
Viacom 82
Virtual Reality 84
Voyager 82

W

Wasserstein Perella 39
Weider Health & Fitness
Wheeling-Pittsburgh Steel 60
WHX 60
Wieden & Kennedy 39
Wilshire Associates 35
Wisconsin Energy 16
Wolf Camera 68
Wrigley 48

Z

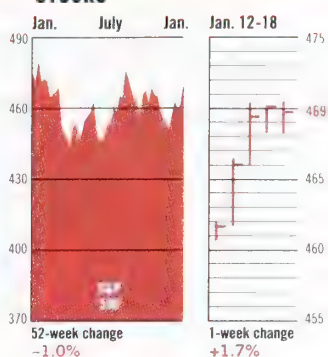
ZZYZX Visual Systems 6

Investment Figures of the Week

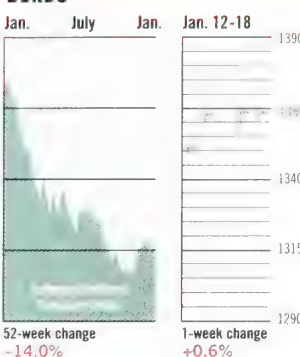
STOCKS

Stocks staged a rally on Jan. 17, led by a surge in the bond market because of an unexpected increase in December sales figures. The industrial average rose nearly 50 points, in the gain since Oct. 28. Interest-sensitive stocks, such as utilities, led the list of gainers. Tech stocks, meanwhile, performed well. But the optimism vanished on Jan. 18 because of concern that the Federal Reserve may boost interest rates. Stocks declined in quake-ravaged Japan.

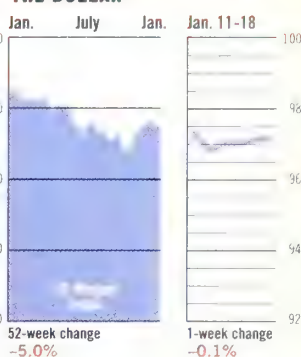
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS

	Latest	% change Week	% change 52-week
DOW JONES INDUSTRIALS	3929.0	1.7	1.1
DOW JONES COMPANIES (S&P MidCap Index)	173.5	2.1	-3.5
DOW JONES COMPANIES (Russell 2000)	252.3	1.7	-3.9
DOW JONES COMPANIES (Russell 3000)	269.3	1.8	-1.5

FOREIGN STOCKS

	Latest	% change (local currency) Week	% change (local currency) 52-week
DOW JONES (FINANCIAL TIMES 100)	3054.9	0.2	-12.1
DOW JONES (NIKKEI INDEX)	19,223.3	-1.7	1.0
DOW JONES (TSE COMPOSITE)	4170.8	-0.4	-8.6

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.85%	5.75%	3.03%
30-YEAR TREASURY BOND YIELD	7.77%	7.84%	6.30%
S&P 500 DIVIDEND YIELD	2.76%	2.80%	2.60%
S&P 500 PRICE/EARNINGS RATIO	17.1	17.0	22.9

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 200-day moving average	457.9	457.5	Positive
Stocks above 200-day moving average	40.0%	34.0%	Positive
Speculative sentiment: Put/call ratio	0.51	0.54	Negative
Insider sentiment: Vickers sell/buy ratio	0.94	1.06	Positive

BLOOMBERG FINANCIAL MARKETS

INDUSTRY GROUPS

WEEK LEADERS

	% change 4-week	% change 52-week
AIRLINES	17.6	-24.2
LEISURE TIME	14.6	0.5
ARMED MARKET AUTO PARTS	11.9	-10.7
CONDUCTORS	11.5	14.4
PUTER SYSTEMS	11.1	33.7

Strongest stock in group

	% change 4-week	% change 52-week	Price
SOUTHWEST AIRLINES	21.7	-46.6	19 ⁵ / ₈
BALLY ENTERTAINMENT	26.1	-19.4	7 ¹ / ₄
ECHLIN	20.4	-3.9	33 ⁷ / ₈
ADVANCED MICRO DEVICES	36.2	66.9	31 ¹ / ₂
INTERGRAPH	25.4	-8.1	9 ¹ / ₈

WEEK LAGGARDS

	% change 4-week	% change 52-week
GENERAL MERCHANDISE CHAINS	-4.9	-14.6
SPECIALTY APPAREL RETAILERS	-3.1	-17.1
WHOLESALESALE	-3.1	2.6
DISTANCE TELECOMMUNICATIONS	-3.0	-14.1
RETAIL MANUFACTURING	-3.0	-3.3

Weakest stock in group

	% change 4-week	% change 52-week	Price
DAYTON HUDSON	-12.9	0.2	69
THE LIMITED	-8.2	2.8	18 ¹ / ₈
FLEMING	-7.4	-11.6	22
AT&T	-4.1	-9.2	49 ¹ / ₂
LIZ CLAIBORNE	-22.9	-23.7	16 ⁷ / ₈

MORNINGSTAR INC.

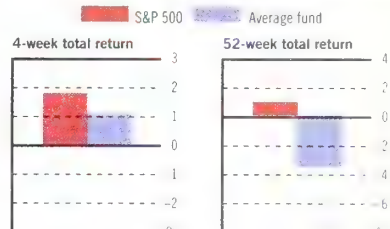
MUTUAL FUNDS

LEADERS

	%
4-week total return	
F&B SPECIAL EQUITIES	10.5
F&B SMALLER COMPANIES	9.8
AGGRESSIVE AGGRESSIVE GROWTH	9.4
52-week total return	
GLOBAL COMMUNICATIONS & INFORM. A	29.0
F&B SMALLER COMPANIES	27.7
BERNSTEIN STEPHENS VALUE & GROWTH	25.0

LAGGARDS

	%
Four-week total return	
WRIGHT EQUIFUND-MEXICO NATL. FID. EQTY.	-37.3
BT INVESTMENT LATIN AMERICAN EQUITY	-23.5
FIDELITY LATIN AMERICA	-23.5
52-week total return	
MONITREND GOLD	-57.3
STEADMAN OCEANOGRAPHIC TECHNOLOGY	-38.9
STEADMAN AMERICAN INDUSTRY	-36.6



RELATIVE PORTFOLIOS

Amounts represent the value of \$10,000 and one year ago portfolio

Figures indicate yearly total returns

Foreign stocks
\$10,660
+0.16%

Money market fund
\$10,488
+0.29%

U.S. stocks
\$10,149
+1.81%

Gold
\$9,839
+1.52%

Treasury bonds
\$8,862
+0.96%

Figures on this page are as of market close Wednesday, Jan. 18, 1995, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are

as of market close Jan. 17. Mutual fund returns are as of Jan. 13. Relative portfolios are valued as of Jan. 17. A more detailed explanation of this page is available on request. r=revised

SIMPLIFYING TAXES WOULD SAVE A BUNDLE

Let's talk taxes. The tax code has become so byzantine that the cost of compliance for individuals and corporations in the U.S. comes to \$75 billion a year—a figure that includes what Americans shell out to accountants and lawyers, the hours taxpayers spend dealing with tax affairs, and the budget of the Internal Revenue Service, according to Joel B. Slemrod, an economist at the University of Michigan.

Keep this huge cost in mind as the Democrats and Republicans fall over each other in the weeks ahead to offer tax goodies. Here's a partial list to date: a cut in the capital-gains tax rate, a child tax credit, expanded individual retirement accounts, homeowners' deductions on losses from house sales, and deductions for college. In short, tax-code social engineering is alive and well in Washington, and every change adds to the cost of compliance.

What a waste. Policymakers should be moving in exactly the opposite direction—toward radical simplification. They should be lowering rates by broadening the tax base through limits on exemptions and deductions. A simplified tax accomplishes two goals. First, it makes political choices transparent. Simplicity removes the social engineering by conservatives or liberals enacted through the tax code. Public spending is made clearly visible on the government's ledger. Second, it reduces Uncle Sam's interference in the affairs of citizens and businesses, permitting markets to work more efficiently.

What exactly would radical simplification entail? There are a number of options. There's the flat tax, favored by Representative Richard K. Armey (R-Tex.), which builds on a plan developed by Hoover Institution economists Robert E. Hall and Alvin Rabushka. This extremely radical scheme

would levy a straight 17% on wages and pensions, with only personal and dependent exemptions. Business couldn't deduct interest or dividend payments, but for individuals, investment income would be exempt. This would end the bias against personal savings currently built into the tax code. In the somewhat related "X-tax" plan of David F. Bradford, an economist at Princeton University, investment income is also exempt from personal tax, but he introduces more progressivity by having rates on labor compensation rise from 15% to 25% to 35%.

We favor a less radical "modified" flat-tax proposal that would be more politically palatable. It would flatten the rate structure into two or three rates and would preserve a few of the most popular deductions, such as home-mortgage interest and charitable contributions. In the early 1980s, Senator Bradley (D-N.J.) and Representative Richard A. Gephardt (D-Mo.) offered a plan with three brackets: 14%, 26%, and 30%. This proposal was designed to keep tax reform from falling too heavily on the poor. Gephardt is now drafting his own flat tax of 10% to 12% for most Americans, with a higher rate for the wealthy. The U.S. was happily headed in this direction with the Reagan tax reform of 1986.

Tax simplification is as appealing now as it was then. It would cut down on tax avoidance and eliminate the need for so many tax lawyers and accountants. It would let individuals and businesses make save-or-spend decisions free from government. And boy, would it save money: A simplified code could cut collection costs from \$75 billion a year to \$5 billion. That's a saving of \$250 billion over five years. Psst! Congress: Want a real tax cut? Clean up the tax code.

WHY WE SHOULDN'T HIKE THE MINIMUM WAGE

To raise, or not to raise, the minimum wage: That is the question being debated in Washington. Both Democrats and Republicans are rolling out their big academic guns to prove that raising the wages of those on the bottom rung of the ladder would (a) boost income and not hurt job creation and (b) boost income and kill job creation. Who knows?

We think the timing is bad for a new tax on labor—which is what a legally enforced, rather than market-induced, hike in wages really amounts to. After two decades of stagnation, real wages are poised to take off on their own, without government interference. Indeed, real wages stopped falling in early 1994 and began rising.

Why the turnaround after 20 years? Productivity. Rising wages have almost always been associated with rising productivity. The 1960s was a decade of high corporate profits, strong 2% annual productivity growth, and hefty pay hikes. The 1990s are beginning to look a lot like that. Profits are up, and productivity growth is running at 3% for the corporate

sector—4.5% for manufacturing—and 1.5% to 2% for the economy as a whole (page 86). Wages can't be far behind.

It is true that the minimum wage (now \$4.25 an hour) is only 35% of the average wage—far lower than the 55% of a decade ago. Those at the bottom clearly have less buying power than in 1985. But it's also true that a much smaller percentage of the workforce labors at minimum wage today than a decade ago. In 1981, 7.8 million workers got the minimum wage—15% of all hourly workers. In 1993, only 4.2 million workers were receiving minimum wage, a mere 6.6% of all hourly workers.

The solution to boosting real wages is not to raise employers' cost of hiring. If Washington wants to fight poverty, the earned income tax credit is a more effective weapon. But economic policies that promote high productivity and fast growth with low inflation are the paths to new employment and, after a lag, higher wages. It happened in the '60s. It's working in the '90s.

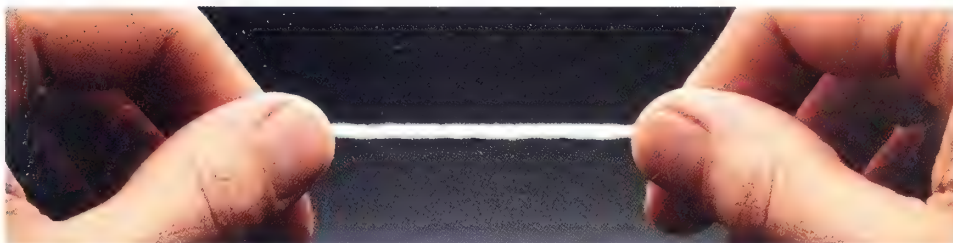
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Step 2.
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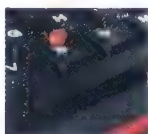


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Let ULTRA FLOSS spring back to its original thickness to brush away plaque.

Introducing Oral-B ULTRA FLOSS, the biggest technological advance in dental floss since, well, dental floss. It's made from interwoven fibers so it stretches thin to fit easily between your teeth, then springs back to effectively remove the plaque that causes gum disease. If only every exercise program that was this good for you was this easy to do. Who else would think of it but Oral-B?



Grisham's pad



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PAGE 108

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ALL SEASON TRACTION





BusinessWeek

FEBRUARY 6, 1995

Cover Story

108 THE BEST MUTUAL FUNDS

Last year was bad for equity funds, but undaunted investors kept pouring money into them. How can you make sure your money is in the right fund this year? By scoping out the data packed into our annual Mutual Fund Scoreboard, now expanded to cover 885 funds. There you'll find '94 return, past performance, investment style, and risk level—among other measures. Pick well

News: Analysis & Commentary

32 MESSAGE FROM THE MARKETS

Rising interest rates have traders fretting that world economic growth will slow—or peter out altogether

34 ON THE PESO PATROL

The knights of NAFTA are facing familiar foes in the battle to shore up Mexico's teetering economy

35 COMMENTARY

Clinton has found a better agenda, and his message has broad voter appeal. What it lacks is a credible speaker

36 GOOD NEWS ABOUT THE IMPORT GAP

Its record-breaking size largely reflects strong U.S. growth and capital investment

37 DETROIT'S ROUGH WINTER

Bad decisions, mostly by Ford, have sent Motown into a temporary skid. But spring should bring a thaw

38 FLASH PROFITS

The quarter's earnings rose an average 46%. Wall Street isn't impressed

38 A NEW LIFE FOR CAT?

At last, both management and the UAW seem serious about ending the strike

42 IN A DITHER OVER DORFMAN

Subjects of the columnist's Wall Street items are threatening to sue—or worse

44 FOR WHOM THE BELL THUDS

Bell Atlantic's interest in privatizing PBS turns out to be more hype than fact

44 A PRINTER FOR ALL SEASONS

Indigo's new system allows for short, customized runs

45 IN BUSINESS THIS WEEK

Bausch & Lomb, Merrill Lynch's plunge, Fidelity, a bias suit, Time Warner and Toshiba, Microsoft, the St. Louis Rams

International Business

52 CHINA

With Deng in deteriorating health, the struggle for power—and over the pace of reform—is already under way

55 JAPAN

Despite the earthquake, signs point to continued economic recovery

56 BRITAIN

For London investment banks, the most lucrative action is in cross-border

58 INTERNATIONAL OUTLOOK

If the center cannot hold, will Germany's left rise?

Economic Analysis

24 ECONOMIC VIEWPOINT

Becker: Maybe the earnings gap isn't such a bad thing

28 ECONOMIC TRENDS

Revisions on U.S. growth, stock market buybacks, threat to Japanese lifeline, employment, U.S. business confidence

29 BUSINESS OUTLOOK

Trade could keep the economy on an even keel



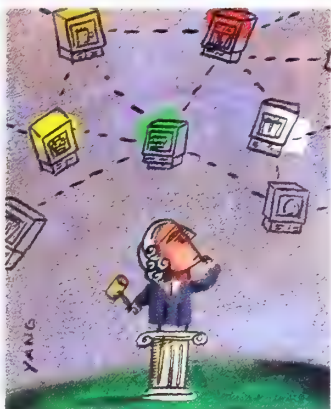
THESE CROSSING
 's passing will leave
 ership unsure of
 or whether—to
 e reform page 52

NOW HEAR THIS
 How two entrepreneurs
 are giving hope to the
 hard of hearing page 152



BOMBARDIER'S BLITZ
 The Canadian company has
 zoomed from snowmobiles to
 jets to Chunnel railcars page 62

EVER STORY
THE HEAP
 ogy funds
 ted the field
 r where
 t performers
 rd to find



CYBERLAW
 The online
 era may be
 rendering
 libel laws
 obsolete
 page 70



BATTERED BOURSES
 Are they signaling a
 global slowdown? page 32

Government
WASHINGTON OUTLOOK
 players change, but gridlock is still
 name of the game
GOP'S BRUTAL BOTTOM LINE
 t will it take to balance the budget?
 , politically agonizing cuts

e Corporation
ADA'S WORLD TRAVELER
 bardier of Montreal has become
 bal presence in a number of
 ing transportation markets
GFIGHT FOR 950 CUSTOMERS
 g corporate jets, the battle pits
 bardier vs. Gulfstream

Legal Affairs
ED WITH A LAWSUIT
 the courts set limits on the
 lom of cyberspeech?

ance
MORGAN'S EMPTIER NEST
 investment bank is gearing up for
 rst major layoffs ever

- 143 INSIDE WALL STREET**
 Big favorites in small-cap stocks
 Giving electric cars a charge
 Brio takes two hefty swigs
- 163 INVESTMENT FIGURES OF THE WEEK**
Social Issues
- 144 THE BASE CLOSED, THE TOWN DIDN'T**
 Tiny Rantoul, Ill., shows how to cash in
 on the peace dividend

- Information Processing**
- 20 TECHNOLOGY & YOU**
 Multimedia: Plug and pray
- 146 I-WAY TIE-UP ON CAPITOL HILL**
 Party politics are killing the prospects
 for much-needed telecom reform
- 147 SMALLER FAMILY, FEWER FRIENDS**
 MCI: A company in search of a strategy

- Science & Technology**
- 149 DEVELOPMENTS TO WATCH**
 Yeast as a guinea pig, materiel "dog
 tags," superconductors, DNA "scissors"
- 150 QUIET STRIDES AGAINST CANCER**
 The immune system is slowly giving up
 its secrets to vaccine researchers

- 151 IMMUNOLOGY'S BOLD NEW THEORY**
 Scientists are rethinking the basics
- People**
- 152 GIVING THE GIFT OF SOUND**
 Two Coloradans have developed a
 promising new type of hearing device

- Personal Business**
- 154 YOUR TAXES**
 A guide to getting through the tax
 trials, including new no-sweat software,
 how to decipher the latest code, and
 planning in uncertain times

- Features**
- 6 UP FRONT**
- 12 READERS REPORT**
- 16 CORRECTIONS AND CLARIFICATIONS**
- 17 BOOKS**
 Lasch: *The Revolt of the Elites and the
 Betrayal of Democracy*
- 161 BUSINESS WEEK INDEX**
- 162 INDEX TO COMPANIES**
- 164 EDITORIALS**
 Helping Mexico is self-help
 The trade deficit: There's a bright side

Up Front

EDITED BY LARRY LIGHT

NEW WORLD ORDER

A COKE WITH THAT KIMCHI?

THE HERMIT KINGDOM MAY soon share a Coke and a smile with the U.S. Washington announced small steps on Jan. 20 to relax the 1950 ban on trade with North Korea, permitting direct phone links between the two countries and allowing American visitors to pay hotel bills with U.S. credit cards. The idea is to encourage further openings by Kim Jong-Il's Marxist redoubt, following last fall's U.S.-North Korea nuclear pact.

If the embargo is eased further, Coca-Cola is one



KIM: Modest openings

company poised to peddle its wares to the North Koreans. The president of Coke's Pacific Group, Douglas Daft, recently hosted North Korea's ambassador to the U.N. at a private luncheon at

FUNNY BUSINESS

THESE 'BANK NOTES' MAY BE DEAD LETTERS

PRIME BANK NOTES, THOSE FAKE securities sold to dupes worldwide, may be headed for the shredder. The Securities & Exchange Commission has charged Trust Group, an outfit that has sold the notes since 1991, with securities fraud. As first disclosed in BUSINESS WEEK, Trust Group bills this paper as debt from the world's top banks, but au-

thorities say it's worthless. By one estimate, investors in the notes have lost more than \$500 million to various scammers. The Manhattan D. A.'s office is conducting a separate criminal probe.

The core of the SEC action involves the Kentucky Association of Counties (KACO), which manages an investment pool for localities. Au-

TALK SHOW "As you from crimes would pardon'd be, let you indulgence set me free."

—Charlton Heston, quoting Shakespeare's *The Tempest* to Congress, in support of endangered funds for the arts

Coke's Atlanta headquarters.

Although American long-distance carriers are now free to start setting up service, it's unclear how long this will take. AT&T says that, while it wants to discuss a deal with Pyongyang, there has thus far been no contact. Company technicians must scout out North Korea's telecom infrastructure to see how to make the linkup. Perhaps, says AT&T spokesman Herb Linnen, they can use an existing undersea cable between North Korea and Japan.

Meanwhile, other countries are stepping up their commercial relations with Pyongyang. The first foreign bank to arrive in North Korea will be Amsterdam-based ING Bank. *Laxmi Nakarmi*

thorities say KACO almost became a victim of the scheme by considering an investment in the notes. Trust Group allegedly promised yearly returns of at least 48%.

Also charged are Lawrence Gerschel, the grandson of financier Andre Meyer, and three associates—securities trader Sandi Kalez and lawyers Jeffrey Moritz and T. Robert Hughes. Says Hughes: "We expect to be fully vindicated." The others did not return calls. *Phillip Zweig*

SLUGFESTS

DOUBLE DUTY IN ORANGE COUNTY

HERE'S A DILEMMA. WITH Orange County mired in bankruptcy, four members of its ruling Board of Supervisors also help oversee its largest creditor. Supervisors William Steiner, Roger Stant, Marian Bergeson, and James Silva sit on the 11-person board of the Orange County Transit Authority, which runs buses and fixes roads. It put \$1.1 billion in the ill-fate county investment pool.

As the California county negotiates a payout plan with creditors, the four will likely be voting both as debtors and creditors. The foursome, who declined to comment on the transit board because of a law requiring supervisor representation.

To OCTA CEO Stan Oftelie there's no problem: Transit and county lawyers have allowed votes in the past where county and agency interest clashed, such as an OCTA suit against the county over liability in bus accidents. The stakes are higher in the bankruptcy arena, but Oftelie says the four can handle both roles fairly. Still, he admits it will be hard for them "not to be personally conflicted." Plus, Oftelie, the chairman of the creditors' committee, says he will be "circumspect" about sharing negotiating strategy with the two-hatters.

A handful of other public works agencies in the county have similar, if smaller, conflicts. Example: Supervisor fill 2 of the 12 board seats of the San Joaquin Hills Transportation Corridor Agency, which is building a 17-mile toll road. *Ronald Grove*



REALITY CHECK

BILL CLINTON, TAX-HIKE CHAMP. That's the Republicans' favorite rap against the President, who lately is trying to recast himself as a tax-cutter. So when New Jersey Governor Christine Todd Whitman gave the GOP response to his State of the Union address Jan. 24, she was sure to slam

Clinton for imposing "the biggest tax increase in American history." Her reference was to the tax hike that Clinton signed in 1993. It will cost \$240 billion over five years, according to estimates from the Treasury Dept. and the congressional Joint Committee on Taxation.



THE GOV

IN REALITY, the Republicans mislead. Only in nominal dollar value was the 1993 tax hike the biggest ever. But the 1982 increase of \$206 billion over five years, signed by Ronald Reagan, comes out to \$268 billion, adjusted for inflation. Looked at another way, as a portion of the overall economy, Reagan still approved

the biggest tax boost in U.S. history. The nonpartisan Congressional Budget Office calculates that the '82 tax hike was 1.3% of gross domestic product, while Clinton's was 0.9%. A private group, the Tax Foundation, also ran the numbers and comes up with virtually the same result. *Paul Magnusson*

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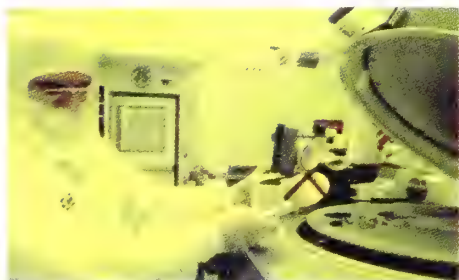
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Up Front

RESEARCH REPORT

MCC CLEANS OUT ITS CLOSETS

IT'S THE GREAT HIGH-TECH sell-a-thon of 1995. Microelectronics & Computer Technology Corp., the privately funded research consortium formed in 1982 to combat Japan's high-tech challenge, is selling off projects. Lots of them.



BACK TO BASICS: An MCC lab

New Chief Executive John McRary wants to make more room for basic research—and put a smile back on the faces of the 20 corporations belonging to Austin (Tex.)-based MCC, ranging from Motorola to Hughes Aircraft. Example: making computers more conversant in plain English.

The overhaul, say the corporate members, is much needed. Before McRary's mid-1994 arrival, they griped when basic research funds were diverted to create start-ups to take technology to market—and bring royalties to MCC. That income would offset declining member support, which caused revenue to drop from \$60 million in 1989 to \$40 million in 1994.

MCC plans soon to sell EINet, a network that supports electronic commerce between companies. The information systems technology from its Carnot Project is being licensed out. And McRary on Jan.

23 sold most of its chip-packaging operation, including an 40,000-square-foot lab and 100 patents, to SI Diamond Technology, an electronic-display maker. The key problem: The technology pipeline out of MCC is far fuller than the pipeline with new projects coming in. *Peter Burrows*

ENDANGERED SPECIES

PROHIBITION FOR PUFFERS?

BIG TOBACCO HAS OPENED A new front against antismoking forces. First came those Philip Morris ads picturing smokers puffing while perched on plane wings. Now there's an academic study,

cigarette maker recently unveiled the study at "21," once a Manhattan speakeasy. In the study, Kean College (N.J.) historian Mark Lender says legal crackdowns on butts, including tax hikes, will bring black markets and organized crime. His evidence: Canada, which saw smuggling from the U.S. after a huge 1993 tax boost made a pack of cigs cost up to \$5. The tax was rolled back last year, and the smuggling subsided. Lender, who is billing B&W \$9,000 for the study, says he has no allegiance to tobacco companies and says he won't testify for them in lawsuits. *Linda Himmelstein*

sponsored by Brown & Williamson Tobacco, linking efforts to curb smoking with the evils of Prohibition.

This year marks the 75th anniversary of Prohibition, and the nation's third-largest

DRAWN & QUARTERED



NEWT'S WORLD

THE NEWT AMERICAN LIBRARY

SPEAKER NEWT GINGRICH HAD to give up his \$4.5 million book advance from a publishing house owned by media magnate Rupert Murdoch. But other publishers are moving to cash in on the flame-tongued Republican's rise to power.

Already, they have pumped out three quickie books inspired by the controversial Georgian. *Quotations from Speaker Newt* contains his philosophical musings, caustic anti-Democratic zingers, and a brief excerpt from his steamy, unpublished spy novel, *1945*. For loyal Newtoids, it also gives a list of Gingrich's "must read" recommendations (example: *The*

Federalist Papers), and a copy of the *Contract With America*.

The other new books at *NewtWit!* (on Clinton: "Dukakis with a Southern accent and *NEWTisms*. Pocket Book which cashed in on the success of the movie *Forrest Gump* with

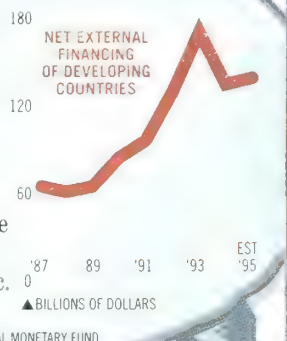


GUMPisms, is hoping for a reprise with *NEWTisms*. Taste: Clinton Democrats at "the enemy of normal Americans." *Richard S. Dunha*

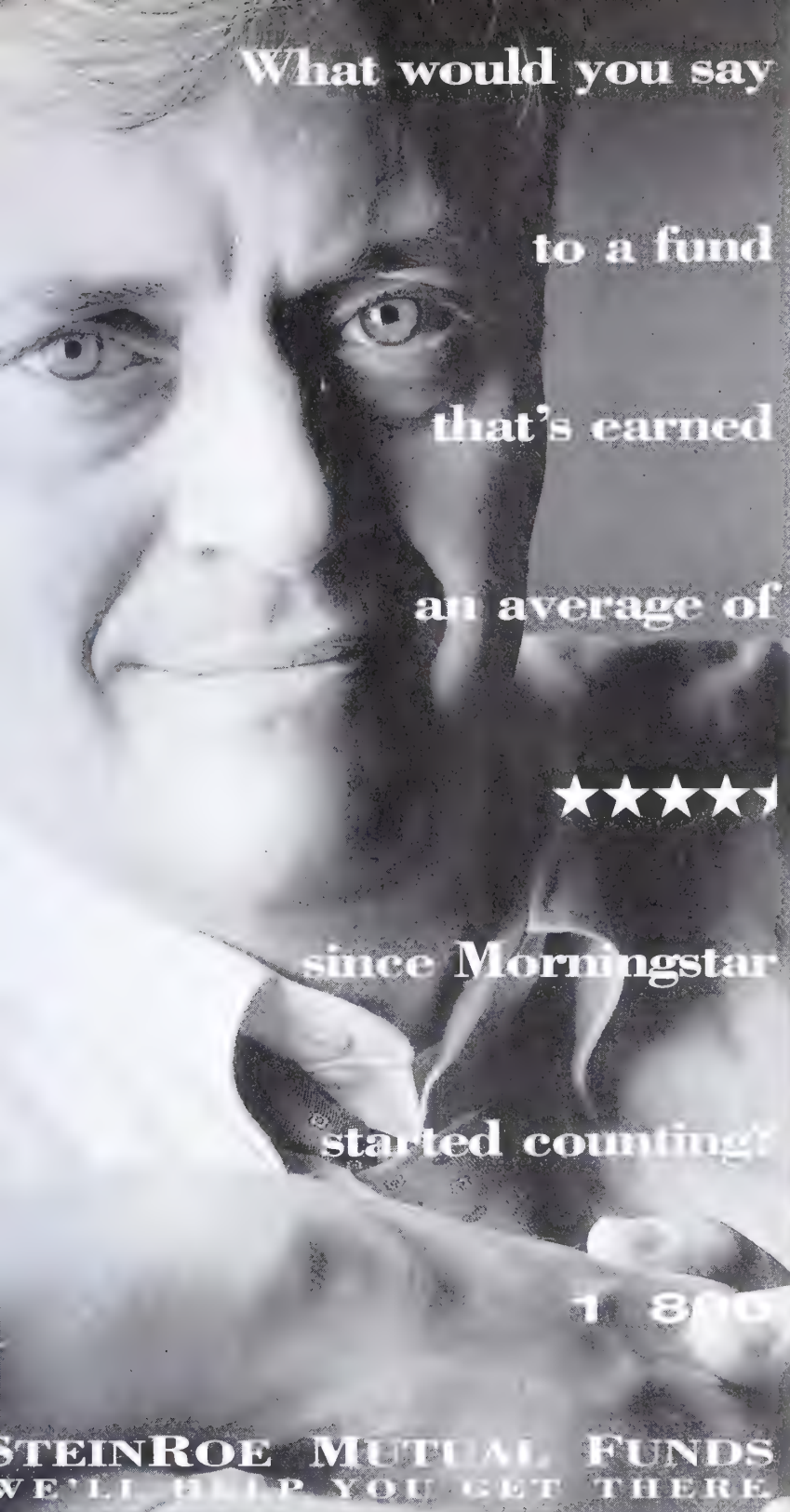
THE BIG PICTURE

THIRD WORLD FINANCING SLOWS DOWN

The popularity of emerging markets soared until last year. Why the dip? One reason: Rising U.S. interest rates in 1994 attracted more capital to America. The Mexico debacle could make even the IMF's modest estimate for this year optimistic.



FOOTNOTES Americans who admit they have discriminated on the basis of others' looks: **58%**



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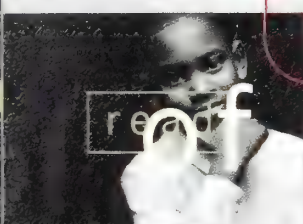
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DON'T READ CONSPIRACY INTO CHECKOUT-SCANNER SLIPUPS

I just read your article "Maybe they should call them 'scammers'" (News: Analysis & Commentary, Jan. 16), about the inaccuracies and overcharging of consumers due to price scanners. I am a loss-prevention and security consultant, and one thing that has amazed me for years is signs at supermarkets stating: "If an item scans higher than the price marked, then it is free."

This offer is shortsighted and inherently has one big problem that hundreds of retailers have failed to recognize. Simply put, the sign should state: "If an item scans incorrectly from the price marked, then it is free." A retailer would rarely find out about undercharges and its own loss without this approach.

Many retailers have not thought out their scanning policies and systems sufficiently to prevent loss as well as promote accuracy. Sometimes technology moves faster than common sense.

Howard Levinson
President
Howard Services
Norton, Mass.

Your article about the errors in pricing when using electronic checkout systems implied that retailers are tilting the error factor in the retailer's favor. As a matter of fact, some 20% to 40% of the pricing mistakes attributed to scanners are, in fact, due to the electrical interference caused by powerful magnetic fields turning on and off, such as from a near-by belt-feed system. This electrical interference can be the source of computer lockups and strange errors that are, unfortunately, more often than not blamed on the operator. It simply is untrue that computers never make errors.

Experience has shown that errors caused by electrical interference will be all over the place—as likely to be in the customer's favor as the retailer's.

But no matter what you say, the scanner and its associated electronic equipment are far more accurate than the old cash register and a tired checkout clerk at the end of the last shopping day before Christmas.

Ben G. Crosby
National Retail Sales Manager
Oneac Corp.
Libertyville, Ill.

I'm in charge of testing all weights and-measures devices in Hamilton County, Ohio. As part of our procedures, we routinely check scanners in grocery, hardware, drug, and convenience stores. Seldom do we find outrageous errors. We do our best to catch the errors through random samples and notify the appropriate corporate officials of our findings.

ADVENTURES IN THE SCAN TRADE

"Experience has shown that errors caused by electrical interference will be all over the place—as likely to be in the customer's favor as the retailer's."

The National Conference on Weights & Measures is just now developing standards for field work on testing scanners in conjunction with the National Institute of Standards & Technology. While 100% accuracy is the ideal as long as humans must enter the information, there will be errors. Our experience is that most businesses will fix any errors we find immediately. And many of them also have a scan-right-or-free policy. In any case, the consumer must still watch at the checkout.

Kevin E. Pyle
Director of Assessment
Hamilton County Auditor's Office
Cincinnati
KEP3@aol.com

How is the consumer to remember the price of each item from the shelf label?

Martha J. Fenn
Brattleboro, Vt.
Continued on page 10

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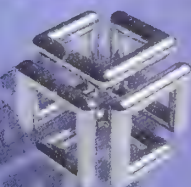


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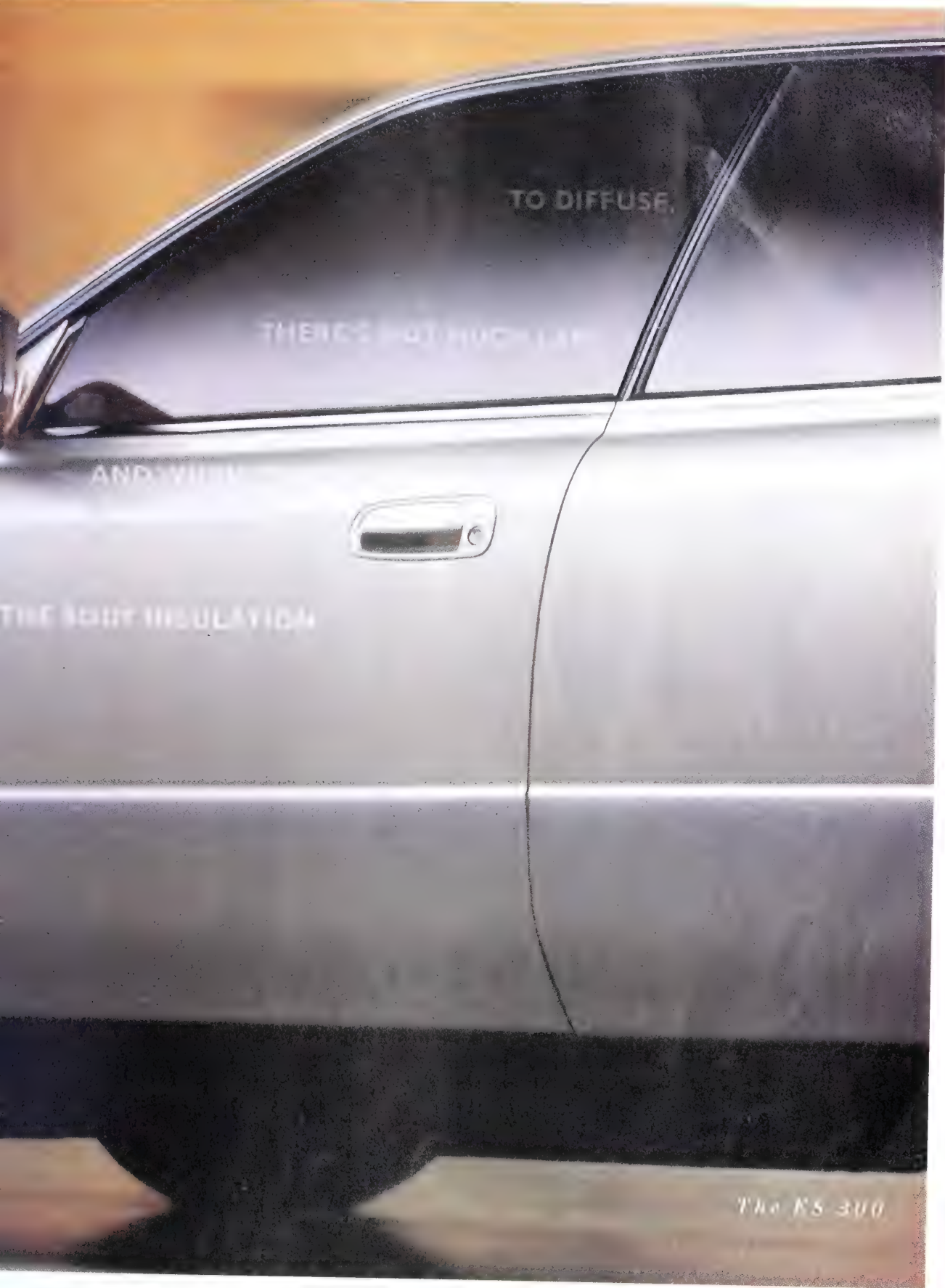
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Readers Report

1998 JUST MAY BE THE YEAR OF THE APPLE

Your article "It just may be the year of the Apple" (Information Processing, Jan. 16), claims that, with the delay of Windows 95, Apple computers might just have an opportunity to capture some market share by means of licensing. However, Apple does not have a real shot at the market with its PowerPC chip because of the large market-share held by the PC. In order for Apple to really move forward, it must be acquired by IBM.

IBM is capable of acquiring Apple and could recapture the market, which would take about three years.

Sujay Shah
Fullerton, Calif.

THIRTEEN PERCENT IS NO DROP IN THE BUCKET

In "Why welfare reform is such a long shot" (News: Analysis & Commentary, Jan. 16), you fluff off total spending on the poor as only 13% of the budget. When did 13% become "only"? I'd call 13% a significant expense deserving close scrutiny and pruning.

David A. Valentino
Vernon Hills, Ill.

A VOTE OF CONFIDENCE FOR ZEDILLO'S PLAN—AND MEXICO

Thanks for your insightful analysis of Mexico's currency crisis, in your article "Mexico: Can it cope?" (Cover Story, Jan. 16). My own prognosis, based on firsthand knowledge acquired during seven business trips to Mexico in the past two years, is an optimistic one.

Yes, President Ernesto Zedillo Ponce de León's plan will be a painful path to prosperity, and it will take time. But it will produce a stronger free-market economy and greater opportunity for bilateral trade among our nations.

Donald W. Nugent
Frankfort, Mich.

BONDHOLDERS COULD USE DIVIDEND REINVESTMENT, TOO

Your article "Buying stocks like clockwork" (Personal Business, Jan. 16) describes some innovative ways investors can make periodic, automatic investments in stocks or mutual-fund shares. For common shareholders, especially of the long-term variety, dividend reinvestment plans, inelegantly called DRIPs, provide an easy, low-cost way to buy more shares, dollar aver-

CORRECTIONS & CLARIFICATIONS

"Colleges must get their financial houses in order" (Readers Report, Jan. 30) should have said Babson College "uses quality-management principles to strive for the highest standards while curtailing waste."

"Susan Powter's wallet gets a nasty workout" (News: Analysis & Commentary, Jan. 23) should have made clearer that the total of \$3.4 million paid to Powter by the Susan Powter Corp. for 1993 and 1994 represents her salary, plus 42.5% of the net profits of the corporation in each year. Also, her bankruptcy petition shows that Powter's legal fees so far amount to some \$184,000. The \$1.7 million mentioned in the story represented legal fees, plus legal claims against Powter.

age, and save, rather than spend, their dividends.

For issuers, DRIPS provide low-cost equity capital and increased shareholder "commitment." Since DRIPS do these wonderful things, why not expand their benefits to the too-often-forgotten investor—the bondholder? Why doesn't some bold company give its bondholders the ability to invest their interest payment in its shares? Let's have D/IRIPS—Dividend/Interest Reinvestment Plans.

William T. Dolan
Minneapolis

BLAMING THE KEYBOARD—AND THE CULTURE—FOR RSI

As a manufacturer of an "alternative keyboard," we commend Linda Himelstein for reporting on the nation's No. 1 job hazard, repetitive stress injury ("The asbestos case of the 1990s?" Legal Affairs, Jan. 16). It's unfortunate that it has to take "megaverdicts" to call the attention of executives and managers to the risks and cost of RSI and the resulting loss of productivity.

When they are part of a comprehensive approach, ergonomic solutions can be relatively inexpensive investments. Private and government studies show the average cost of an ergonomic modification to a workstation (e.g., keyboard, chair, and/or training) is about \$250. This is a small price to pay next to the average RSI workers' compensation case cost, reported in the range of \$8,000 to \$14,000 each.

Gerald C. Groff
President
Marquardt Switches Inc.
Cazenovia, N. Y.

Please excuse a handwritten letter but due to a repetitive stress injury and under doctors' orders, I'm presently not allowed to touch a keyboard. Also, excuse me if I take exception to your story. Blaming keyboard manufacturers isn't the answer.

With fewer employees handling heavier job loads, frequent breaks are often not options until the damage has been done. Common sense dictates that job tasks should be structured so as not to put anyone at risk for these painful and debilitating injuries. Knowing when to stop doesn't enter into the picture if expectations are unreasonable and workstations are not ergonomically correct.

Kristine Voigt Cohe
Boston

WHY THE HOOPLA ABOUT THE BULLETS' BOX OFFICE?

I found the recent article "Meet the fastest five-footer in the NBA" (Sport Business, Jan. 16), about Susan O'Malley of the Washington Bullets, a little confusing. Let me get this straight: The Bullets average only 69% capacity for their home games with the hottest sport in America, and she's considered to be doing a good job? "Impressive," you said.

Please forward my resumé to Ab Pollin immediately. In a town like Washington, with no baseball team, hockey team on strike, and a lousy football team that finished its season in December, to be satisfied with 5,800 plus vacant seats every night is no "impressive."

R. K. Bake
Danville, Ill.

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THE REVOLT OF THE ELITES
AND THE BETRAYAL OF DEMOCRACY

Christopher Lasch
London • 276pp • \$22

A SKEWED VIEW OF WHAT AILS AMERICA

Americans are fearful about the future. Ethnic rivalries divide communities. Government is unduly. Public schools are failing, the big trade is flourishing, and violent crime seems omnipresent. The middle class is losing job security in the competitive global economy. To social critic Christopher Lasch, who died last February, America's problems seemed so tractable that in his final book, *The*

Revolt of the Elites and the Betrayal of Democracy, he wonders whether democracy has a future. At the moment of its dazzling triumph over communism, democracy is being under heavy fire at home," he writes, "and democracy is bound to increase if things continue to fall apart at the present rate."

What has gone so awfully wrong? America's social decline was back-in-trade for Lasch, who burst into prominence in 1979 with *The Culture of Narcissism*, a bleak portrait of Americans as self-absorbed and self-aggrandizing that greatly influenced then-President Jimmy Carter. But in this timely but ultimately unsatisfying new book, Lasch has focused on a fresh evil.

Democracy is threatened, he says, by the rise of an educated elite who are at home in a global economy linked by computer, modem, and fiber-optic cable. These are people who thrive in "a world of abstract concepts and symbols, ranging from stock market quotations to the ideal images produced by Hollywood Madison Avenue, and who specialize in the interpretation and deployment of symbolic information." Unlike the traditional middle and working classes, this

group has seen its earnings rise over the past 20 years, he says. Its members belong to "the fortunate fifth"—the 20% of the populace who control half the country's wealth.

Yet Lasch's real concern is not economics but values and culture. Members of the new aristocracy of brains, he asserts, have made a stunning break with past elites: They don't care about Middle America and the working poor.

Their loyalties are not national. American members of this elite are more comfortable with their peers in Jakarta or Buenos Aires than mingling with the bourgeoisie at home, whom they perceive as reactionary, sexually repressed, and middlebrow. And since they pay for private schools, private police, and other private services, they have no sense of civic attachment or public service. This analysis echoes

1991's *The Work of Nations*, in which Robert B. Reich, now Labor Secretary, also depicted a professional and managerial elite poised to skim the cream from the global economy—and forget their obligations to less talented Americans.

What Lasch wants to see is a return to a kind of Jeffersonian democracy, a society of neighborhoods, a culture of personal responsibility, and a more equitable economy. Politics, which he sees as too tolerant and technocratic, would be vigorous and passionate. As in his earlier *The True and Only Heaven*, Lasch is proselytizing for a civic populism that embraces religion, rejects the welfare state, and limits the free market—because unrestrained market forces, in his view, destroy communities. Everyone, he believes, requires the "character-

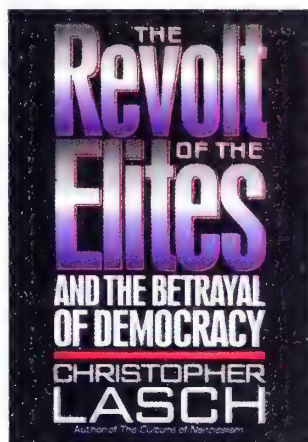
forming discipline of the family, the neighborhood, the school, and the church, all of which (not just the family) have been weakened by the encroachment of the market."

Within the context of "the revolt of the elites," Lasch touches on a remarkable range of issues preoccupying people these days—the consequences of growing inequality, the fraying of national cohesion by multiculturalism, the evasion of personal responsibility. Unfortunately, the book is often superficial and annoyingly written. Arguments tend to meander or dwell on obscure academic debates. Much analysis is marred by sweeping generalizations and cranky, weakly supported observations. Often, the book simply disappoints—as when Lasch calls for a politics that more directly confronts such controversial issues as affirmative action and abortion but remains vague about just what that would entail.

Worse, the evidence for a "revolt of the elites" is shaky at best. An aspect of the problem is the shrinking of the middle class around the globe, Lasch asserts—but in fact, from Poland to Argentina, vibrant middle classes are emerging. Certainly, there is no more troubling economic phenomenon than the rise of income inequality in America over the past 20 years—yet the discrepancy is far from unprecedented; Lasch simply tinges earlier generations with the glow of nostalgia. He ignores how information technologies such as the Internet are fostering new—and potentially inclusive—forms of communications and communities. And he underestimates today's political ferment. Far from dodging controversy, the nation has been intensely debating federalism, mandates, welfare, constitutional amendments, and public spending for years.

In tracing America's current malaise to the emergence of a dangerously insulated elite, Lasch is not persuasive. As a result, his warning that democracy is imperiled doesn't ring true. But for all its flaws, *The Revolt of the Elites* keeps raising important questions—about the impact of the global economy on society, about the legacy of acquisitive individualism, about the demands a flourishing democracy makes on its citizens.

BY CHRISTOPHER FARRELL
Farrell is a *BUSINESS WEEK* economics editor.



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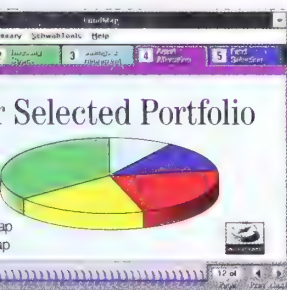
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BY STEPHEN H. WILDSTROM

CD-ROM UPGRADES: PLUG AND PRAY

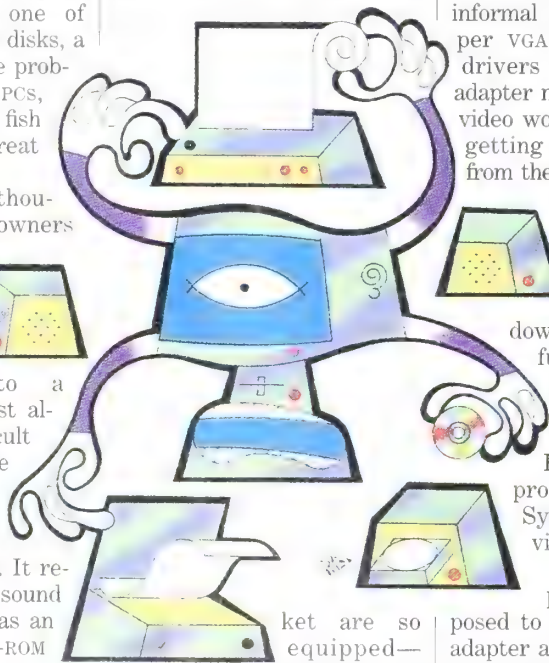
The other day, I popped a CD-ROM drive into the Macintosh in my office. The whole operation took about 10 minutes. And best of all, when I turned the power back on, I was ready to go—no configuration programs, no baffling questions about “IRQ numbers” or “I/O base addresses.” After a quick test, I popped in one of Sumeria’s Ocean Life disks, a CD that had given me problems on Windows PCs, and happily watched fish swim around the Great Barrier Reef.

As hundreds of thousands of computer owners who bought “multimedia upgrade kits” for Christmas have discovered, adding equipment to a Windows PC is almost always far more difficult than for a Mac. The physical installation in a PC isn’t terribly difficult if you can handle a screwdriver. It requires plugging in a sound card, which doubles as an interface for the CD-ROM drive, slipping the drive into the computer, and hooking up some cables.

DELAYED CRASH. The configuration programs, on the other hand, are baffling. But unless your setup is complicated by the presence of a network or a scanner (a problem I’ll address in a future column), accepting the answers the program suggests for its own incomprehensible questions usually works.

The real trouble often starts once the hardware is connected. Maybe the soft-

ware crashes halfway through the setup process. Or it installs, but the program crashes later. Or the video clips don’t work. Or the colors look weird. Even buying a computer with a CD-ROM drive and sound card installed—and according to Compaq Computer Corp., 75% of the machines sold to the home mar-



ket are so equipped—will not ensure multimedia success.

What could? Hopes are high that the long-awaited new version of Windows due later this year will at last give the “plug-and-play” capability Mac users have come to love. But a look under the hood of your PC suggests that it will take more than Windows 95 to cure those multimedia blues. The problem usually lies with an obscure bit of software called a “display driver,” the code that translates program instruc-

tions into the thousands of colored dots, or pixels, that appear on your monitor. Symptoms of a video driver on the fritz can range from colors that don’t look right to malfunctioning printers.

Unlike the Macintosh world, where Apple Computer Inc. has defined the standards, Windows is a competitive free-for-all. The only Windows video standard really supported by Microsoft Corp. is a lowest common denominator called VGA, which offers a 640-by-480 pixel display with just 16 colors. Most multimedia programs need at least 256 colors.

DRIVER ED. For higher resolution or more colors, there’s an informal standard called “super VGA” that depends on drivers supplied by video-adaptor manufacturers. Many video woes can be solved by getting the latest driver from the company that made your video adapter or computer, often not an easy task. It took me two weeks to find, download, and successfully install the update needed to run a preliminary version of Microsoft’s Bob (BW—Jan. 30) properly with an STB Systems Inc. Horizon video adapter.

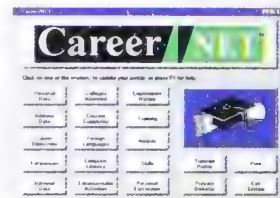
In Windows 95, plug-and-play is supposed to identify your video adapter and automatically install the right driver from an extensive list supplied by Microsoft. That should help a lot. But here’s the catch. The improvement will only last if both display-adaptor manufacturers and multimedia programs live within the rules of Windows 95 better than they did with the admittedly inadequate existing Windows standards. Otherwise, it won’t take long before the current multimedia chaos is recreated with a new operating system—and Macs will look better than ever.

BULLETIN BOARD

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GRADS FOR HIRE

It’s getting to be that time of year, when flocks of corporate recruiters descend on hordes of job-hungry seniors. Technology won’t guarantee success for either job-seekers or companies, but it can make the process simpler and more orderly.



Career/Net from I/Net Inc. (800 403-0562) offers a Windows program that asks students questions and assembles the answers into an electronic resumé (which can also be printed out as an attractive paper document). The information is assembled into a database that is distributed to subscribing businesses on CD-ROM. Students pay \$100 for the service. The company is distributing the database free to the top 200 employers in each state; smaller companies can subscribe for \$495 a year.

MAPS FOR MARKETING

If you need the ultimate in pinpoint demographic information, Claritas Inc., based in Alexandria, Va., has the product for you. Catalyst GIS+ marries Claritas’ demographic marketing information with mapping software from MapInfo Corp. The result is a visual display that shows income and other characteristics down to the census-tract level. The CD-ROM package, priced from \$20,000, is designed for businesses such as retailers and direct marketers.



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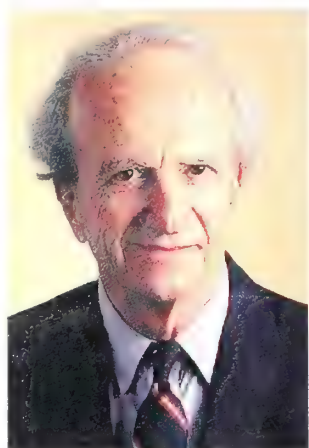


Computer Systems



BY GARY S. BECKER

MAYBE THE EARNINGS GAP ISN'T SUCH A BAD THING



CARROT:
The gap may even spur growth. As companies bid up wages for skilled employees, others are led to invest in more training

Income inequality grew substantially during the Reagan and Bush Presidencies, yet the midterm elections suggest voters did not hold this against the Republican Party. The reason may be because they realize that the increase in inequality is related to economic growth. When greater inequality is due to higher rates of return on human capital and other investments in knowledge, it can be an engine that drives an economy toward more rapid economic growth.

Ever since Jean-Jacques Rousseau's *Discourse on the Origin and Foundations of Inequality* (1755), the emphasis has been almost exclusively on the negative aspects of income inequality. But in modern economies, growth requires an educated and trained labor force, since production of computers, other electronics, and most manufactured goods and services needs knowledgeable workers. An economy grows faster when rates of return on investments in human capital increase, or when the amount invested expands.

The increased earnings gap during the past two decades in the U.S. is mainly the result of higher returns on education, training, and experience. This didn't happen because of Presidential or congressional policies but because companies competing for skilled workers bid up their pay compared with the wages of less-skilled workers.

GRADUATION GIFT. Starting in the 1970s and continuing unabated until the end of the '80s, the gap between the weekly earnings of college and high school graduates rose from about 40% to some 70%, while the premium on completing high school pushed up to over 30%. Similar trends raised the compensation of older and more experienced employees compared with that of younger and newer workers. These trends toward higher benefits from knowledge slowed during the past few years, but they have not reversed direction.

Most Western European countries experienced related trends in earnings differences by education and job skills. Labor markets are not as flexible there, so the gap in weekly earnings between more and less knowledgeable employees rose less in Europe, while unemployment rates of younger and other less trained workers increased much more than in America.

The widening inequality in earnings and the buoyant demand for skilled workers also indirectly encourages greater growth in the

economy by increasing the incentives for young people to invest in themselves. That's one reason why government data shows high school graduation rates of blacks in the U.S. have risen substantially since the late 1970s to the point that they are now close to the very high rates of whites.

HIGHER ENROLLMENTS. And despite the rapid increase in college tuition since 1980, the fraction of male high school graduates who continued their education grew by several percentage points, while college enrollment rates of women expanded even more rapidly. Students from poorer families were hurt by cutbacks during the 1980s in federal grants to college students, but a study by Thomas J. Kane of Harvard University shows that college enrollment rates of blacks rose sharply during the latter part of the 1980s after falling earlier in the decade.

Unfortunately, the higher returns on human capital have been associated with deteriorating earnings for persons at the bottom of the economic ladder. Real earnings of high school dropouts and others with few skills not only declined relative to more educated and trained employees but also fell by a lot in absolute terms. This explains why the labor-force participation rates of unskilled groups have dropped noticeably since the latter part of the 1970s while the number of jobs have expanded dramatically.

This makes it even more essential to help young persons from poorer families overcome any artificial obstacles to improving their education and training. State, local, and federal governments can help with policies that do not require greatly increased public spending. States can improve the quality of high schools in low-income neighborhoods by raising the competition among schools for students. I believe the best way to accomplish this is by offering tuition vouchers to students from poor families that they can use at private as well as public schools.

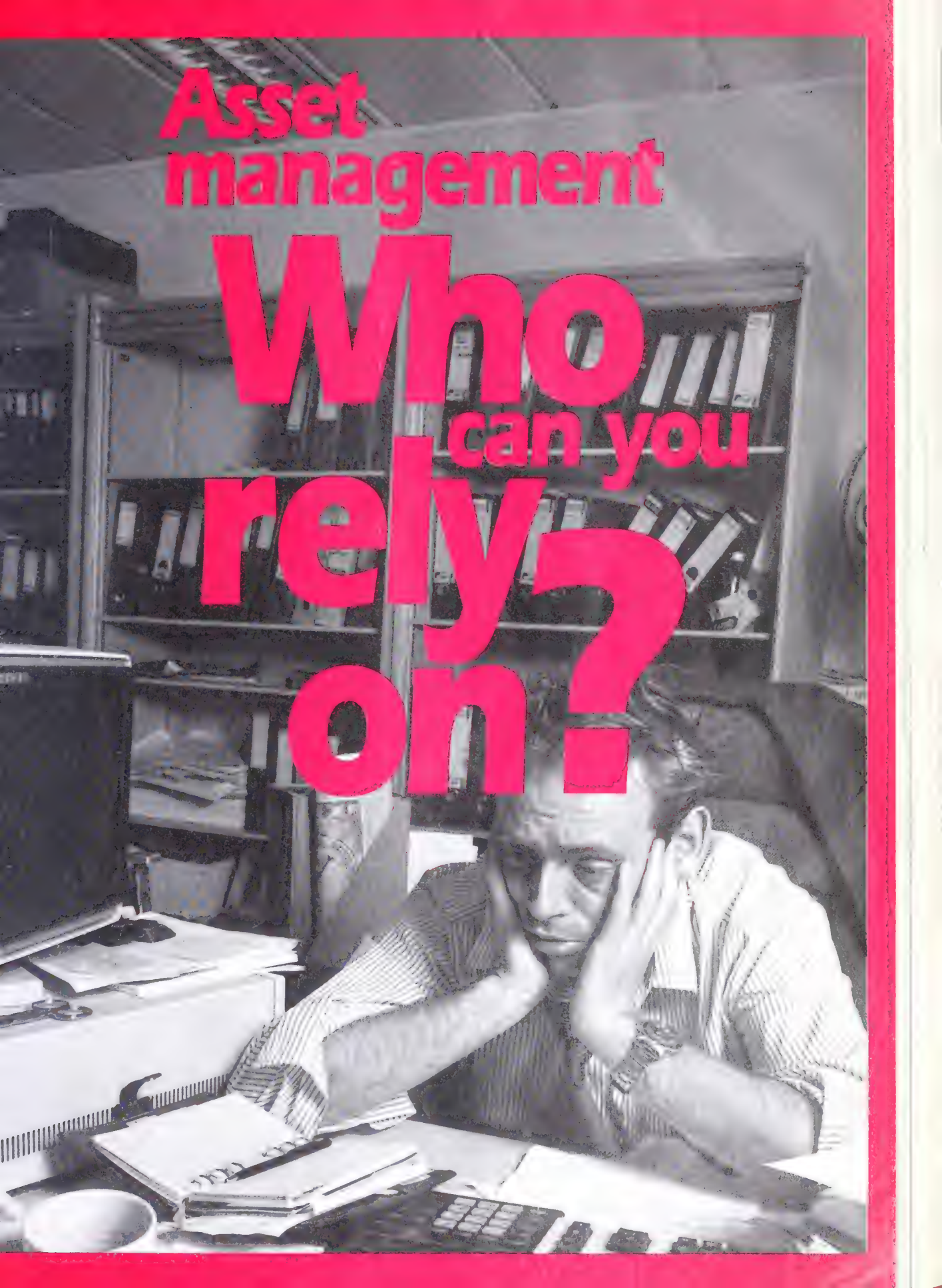
The federal government has a limited but valuable role to play in raising skills. Its loan program to college students should be expanded. At the same time, however, strenuous efforts are needed to reduce the embarrassingly high delinquency rate on past loans to students.

Everyone, from government to the intellectuals, must rethink the pluses and minuses of income disparities.

Gary S. Becker, the 1992 Nobel laureate in Economics, teaches at the University of California, and is a Fellow of the

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INSURANCE & INVESTMENT

BY GENE KORETZ

HOW FAST IS THE U.S. GROWING?

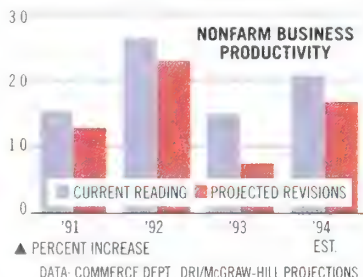
Revisions will show less oomph

A lot of economic observers think that U.S. productivity growth is finally on a roll. Not only did it hit a 20-year high in 1992 but it has now risen by at least 1.5% for four straight years—the first such string of gains since the 1960s.

What's puzzling is that this impressive record has yet to raise the living standards of many Americans. The Census Bureau reports that real median family income declined steadily from 1990 through 1993, for example, and real median earnings of full-time year-round workers fell in 1993, as well.

A new study by economist Mark J. Lasky of DRI/McGraw-Hill seeks to resolve this seeming contradiction. It sug-

DOWNSIZING AHEAD FOR U.S. PRODUCTIVITY GAINS



gests that a big part of the answer lies in the statistical method used to calculate gross domestic product, which tends to exaggerate recent hikes in investment, productivity, and economic growth.

The government uses a fixed-weight method to calculate GDP. That is, it uses the expenditures in a particular base year (currently 1987) to measure the real prices of individual components of GDP and thus their contribution to overall output. This method has many advantages, but one big disadvantage: It gives too large a weight to pieces of output whose prices lag behind overall inflation after the base year.

The problem is especially troublesome when, as in recent years, investment has been heavily concentrated in computers, whose prices have been falling rapidly. Under the fixed-weight method, the purchase of a \$1,000 computer today that has the same computing power as a \$10,000 workstation in 1987 would be

counted as a \$10,000 expenditure. Yet its actual impact on overall economic activity would be similar to \$1,000 spent on other items, whose prices may have risen. To lessen such distortions, the government issues a comprehensive revision of GDP data every five years, using a more recent base year.

The next such revision, which will shift to 1992 as the base year, will occur in the summer of 1996. But economists have already begun to calculate what it may reveal. Dean Baker of the Economic Policy Institute says it will show that investment in the current expansion has been substantially overstated.

DRI's Lasky estimates that growth in 1992 and 1993 may be reduced by an average 0.5% a year. And annual productivity gains during the expansion will be cut by about 0.45% (chart). These downward revisions help explain why income and employment growth have been so sluggish relative to output.

Although productivity growth so far in the 1990s will be lowered, the good news is that the economy has more breathing room for noninflationary growth than recent measures of GDP suggest. And the long-heralded productivity breakthrough may still lie ahead.

THE PROFITS IN STOCK BUYBACKS

Some augur future price rises

Keep your eye on companies announcing plans to repurchase their own shares on the open market. A National Bureau of Economic Research study by David Ikenberry, Josef Lakonishok, and Theo Vermaelen, finds profitable opportunities in such news.

In an analysis of stock movements on the major U.S. exchanges from 1980 through 1990, the economists found that prices of stocks named in repurchase announcements rose by an average of about 3.5% relative to the market in the days immediately following the news releases—a modest increase. If held over the next four years, however, a significant number yielded returns averaging some 45% more than the market.

The high performers were so-called value stocks, the fifth of the repurchase group with the lowest prices relative to book value. On the other hand, glamour stocks, which enjoy high price-to-book-value ratios, failed to outperform the market over a four-year period.

In short, when companies with low prices relative to book value explain

their repurchase plans by claiming that their shares are "undervalued," they are often telling the truth.

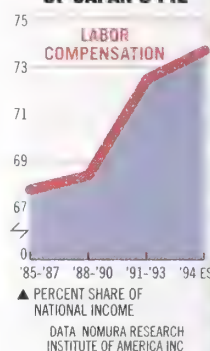
A BIG WORRY FOR JAPAN INC.

Is lifetime employment at stake?

Economist Juichi Wako of Nomura Research Institute notes that Japanese labor's share of national income has shot up from about 68% through most of the 1980s to a new high of around 73% in recent years (chart)—about the same share of the pie as that of U.S. workers. Because the trend occurs at a time when Japanese economic growth has slowed sharply, Wako believes it reflects determination to keep lifetime employment systems intact.

And therein lies a dilemma. Japan may have benefited from benign employment practices in the past, but its increasingly sluggish growth suggests they are becoming counterproductive. Companies that wish to survive in a more competitive world, says Wako, may soon find that they can no longer afford to maintain commitments to lifetime employment.

WORKERS GET MORE OF JAPAN'S PIE



U.S. BUSINESS STAYS UPBEAT

Confidence indexes keep rising

Measures of U.S. business sentiment still point to strong growth. Dun & Bradstreet Corp.'s latest nationwide survey of executives shows rising hopes for sales, profits, and hiring in this quarter. Indeed, indexes of price expectations and employment intentions hit their highs for the current expansion.

Meanwhile, the National Federation of Independent Business reports that small-business optimism surged to a cyclical high during the fourth quarter, as did capital-spending plans. December's hiring plans also stayed near record levels. The political climate hasn't hurt, since the NFIB helped shape the GOP's Contract With America.

JAMES C. COOPER & KATHLEEN MADIGAN

TRADE COULD KEEP THIS SHIP ON AN EVEN KEEL

U.S. ECONOMY

The economy will take on a new personality in 1995. It's your choice. The Federal Reserve is forcing the change as one of the fastest tightenings of monetary policy in U.S. history. As a result, the economy's Clint Eastwood of last year will become this year's Caspar Milquetoast. And a key determinant in how well the economy does in 1995 will be the performance of 1994's frailest sector—foreign trade.

Higher interest rates will rein in last year's growth in many sectors, the economy's interest-sensitive sectors. In 1994, spending on consumer durables, business equipment, and housing—a fourth of real gross domestic product—accounted for half of the economy's growth. Not this year.

EXPORT A RECORD SHARE OF OUTPUT



Against that backdrop, foreign trade becomes a central theme in the 1995 outlook. Last year, a widening trade deficit stole nearly a full percentage point from economic growth. This year, trade will go a long way in determining the Federal Reserve's success or failure in bringing this overheating economy down for a soft landing.

PROGNOSIS for trade in 1995 looks considerably better than last year's dismal showing. Of course, it could be hard for it to get much worse.

In November, the trade gap for all goods and services widened to a larger-than-expected \$10.5 billion, from \$9.5 billion in October. Exports rose 2.2%, but imports rose 2.5%. The November gap comprised a \$15.6 billion deficit in goods and a \$5 billion surplus in services. For goods only, the 1994 deficit appears headed for a record (page 36).

However, the fourth quarter may well mark the trade deficit's turning point for this business cycle, at least when measured in real volume after adjusting for import and export prices. Import growth will slow as the economy cools off, and exports will grow at a double-digit pace, as

Europe continues to recover and as growth in the rest of the world remains buoyant. The result: a shrinking trade deficit that will add to economic growth, not subtract from it.

Real exports should accelerate from 1994's 9% pace. Amid major productivity gains, falling unit labor costs, and a weaker dollar against some of our key trading partners, U.S. manufacturers are poised to take advantage of faster global growth. That's especially true in emerging markets, where infrastructure and investment needs fit perfectly with the strong capital-goods profile of U.S. exports.

One growing uncertainty in the export outlook, however, is the fallout from the Mexican crisis. The peso's plunge will cut deeply into Mexican demand for imported goods. Last year, Mexico bought 10% of U.S. goods exports and, at yearend, U.S. shipments headed south of the border had grown about 30% from a year ago, aided by the North American Free Trade Agreement. Taken by itself, a sharp slowdown in Mexican demand will not cut deeply into U.S. exports, but the risk is that the financial turmoil could spread to the rest of Latin America and beyond.

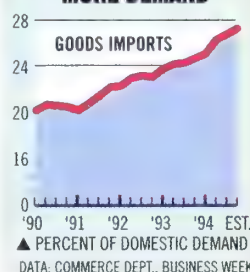
Even north of the border, currency troubles exist. The Canadian dollar has fallen to a nine-year low vs. the U.S. dollar. That means the U.S. currency is exceptionally strong against two of its three largest trading partners, a situation that works against U.S. trade improvement because it encourages imports and discourages exports.

As the case with Canada and certain European countries shows, the global financial markets are making it clear that any nation with high debt and fiscal problems is an increasingly less attractive destination for capital. That will force tighter fiscal policies, higher interest rates, and slower global growth, which could limit U.S. export gains.

THE TROUBLE with trade in 1994, however, was imports. Last year, real imports surged by 15%. Although we now export a record 23% of our goods output, we also import a record 27% of the goods we buy (charts).

However, this increased openness of U.S. trade has a bright side for the outlook. Increasingly, the foreign sector is acting as a stabilizer for U.S. growth during periods of boom and bust. As domestic demand picks up relative to

BUT IMPORTS SATISFY MORE DEMAND



foreign demand, the deteriorating trade balance helps to prevent the economy from overheating. In 1995, just the opposite will occur: A shrinking deficit will buoy the economy, largely because the slowdown in domestic demand is expected to cut import growth by about half.

Moreover, much of last year's inventory buildup was imports. That means that as businesses scale back their need for inventory this year, cutbacks in ordering by retailers and wholesalers will not fall completely on U.S. manufacturers. Foreign producers will share the pain.

IMPROVEMENT in the trade deficit this year will not come fast, though. So far, there is only scant evidence that interest-rate hikes are slowing domestic demand. December housing starts did fall 1%, to an annual rate of 1.53 million, but that followed a 7.6% jump in November. And starts of single-family homes actually rose 2.8%. Permits to begin new construction also increased, although unseasonably mild weather may have boosted activity.

Early-bird reports from retailers on January sales look upbeat. Seasonally adjusted sales at department and chain stores through the third week of the month rose a solid 2.4% from December, says *Johnson Redbook Report*. Buying from a year ago is up a sturdy 10.4%. That's not surprising, however, given that half of the country was covered in snow and ice this time last year.

Moreover, corporate profits appear to have posted yet

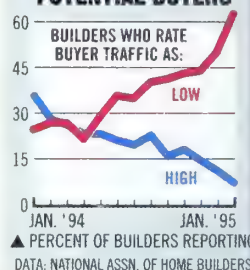
another stellar performance in the fourth quarter, according to *BUSINESS WEEK's* first look (page 38). Strong profits will continue to generate the cash flow necessary for businesses to increase their outlays for new equipment.

But as the year wears on, the economy's person gradually will begin to change. Already, carmakers are sounding a cautionary note. Ford recently announced production cuts in three of its vehicles because of softer demand. And housing, always the first sector to show the effects of rate hikes, is looking weaker.

Mortgage applications to buy a home dropped to a three-year low in mid-January. In addition, a January survey of homebuilders paints an increasingly dim picture. Since July, traffic of potential buyers has all but dried up, says the National Association of Home Builders (chart). And twice as many builders now rate buying conditions as "poor."

As the soft landing begins to gel in response to the Fed's attempt to throttle back domestic demand, think of the improving trade deficit as a flight insurance. A slower pace of imports, combined with better export growth, will lessen the chances of crash landing.

BUILDERS SEE FEWER POTENTIAL BUYERS



EUROPE

IN BRITAIN, FAST GROWTH... AND INFLATION FEARS

Britain ended 1994 with a bigger-than-expected bang. And this year looks as if growth will continue but at a slower pace, if the Bank of England has its way.

Britain's real gross domestic product grew at a strong 3.1% annual rate in the fourth quarter.

For the year, the economy expanded by 4%—the biggest annual gain in six years. The job market also showed signs of momentum as the year ended. In December, unemployment fell by 54,600—the largest monthly drop in six years. The jobless rate slipped from 8.8% to a three-year low of 8.6%.

Looking ahead, manufacturers expect 1995 to bring further

growth but higher prices. The Confederation of British Industry's Jan. 24 survey shows that business optimism rose in January, helped by expectations of stable output growth and strong export orders.

However, the CBI also found that 41% of companies plan to raise prices within the next four months, while only 8% expect to lower prices. The net reading of 33% is the highest in five years (chart). Businesses reported higher unit-production costs and tighter capacity use.

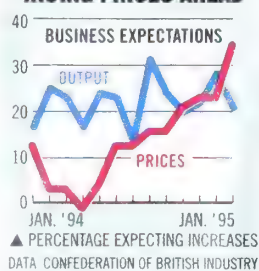
These price pressures are raising worries about rapid inflation—long a scourge to Britain's economy. As a result, the Bank of England will

continue to tighten monetary policy. The BOE has hiked interest rates twice since September, and the strong GDP and CBI reports raise the odds for another boost soon.

The government is also pursuing restraint on the fiscal side. Higher excise taxes on tobacco and alcohol kicked in on Jan. 1, and extra social security payments, scheduled for April, have been tabled. Both measures will cut into household disposable income.

The BOE's goal is to slow the economy, not strangle it. By raising rates now, while inflation is a modest 2.9%, the central bank hopes to keep Britain's economy growing, but at a slow enough pace to avoid the capacity and labor constraints that have historically pushed inflation to double-digit levels. In the BOE's view, less is sometimes more.

STEADY OUTPUT, BUT RISING PRICES AHEAD



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FUNDS**

[\$17 billion in assets]



Battered bourses around the world may be foretelling a global slowdown

A currency crisis in Mexico. An earthquake in Japan. War in Russia. Rising political tensions in China. Mounting budget woes in Canada and Europe. Any one of these events might be enough to ruin a global investor's portfolio. But there's even more bad news in sight. In addition to all the other stresses on world markets, add one more concern: the specter of ascending interest rates around the globe. And that has traders fretting that economic growth will slow—or pe-

As a result, stock markets from Toronto to Taipei are getting whacked. In the past three months, European markets have suffered a steady decline. Bourses in other parts of the world are faring even worse. Mexico's stock market has fallen 54% in dollar terms. Japan's Nikkei stock average is off 11.1%, and Hong Kong's Hang Seng Index is down more than 21.7%. Trading on Moscow's fledgling stock market has dried up. And the Dow Jones industrial average is treading water. Around the world, says Morgan Stanley & Co. strategist Barton M. Biggs, "there's been a huge loss of faith" in equities.

INFLATION FEARS. What makes this failure of confidence so puzzling is the current good health of the global economy. After a robust 4% spurt last year, U.S. gross domestic product may expand a further 3.8% in 1995, estimates Morgan Guaranty Trust Co. Paced by a German recovery, Europe may grow by 3.2%, and Japan could expand more than

2% despite the shock of the Kobe earthquake. Even Mexico's peso collapse probably won't extinguish growth altogether in Latin America.

But stock traders are looking straight through the good news. Why? To Pete Sullivan, European strategist for Merrill Lynch & Co. in London, traders "have already taken account of a strong earnings recovery. Equities are pretty full-valued." That allows them to focus on their worst fears: The likelihood that the Federal Reserve will see the strong growth projections as justification for intensifying its year-long battle against inflation. Traders thus see a sharp hike in the federal funds rate—perhaps by 5 basis points—as soon as Jan. 31. Many investors also expect additional increases in the U.S. and across the industrial and emerging world stretching into next year.

By the time they peak, short-term U.S. rates alone could be as high as 8%, figures Morgan Guaranty economists

William A. Brown. The prospect of a global liquidity squeeze is already prompting some economists to erect a new wall of worry as they tone down growth and earnings estimates for 1996 and beyond. Smith Barney Inc. international economist J. Paul Horne, for one, thinks the U.S. economy will brake to a 1.6%-a-year crawl by next year, followed in short order by a "modest" European recession stretching into 1997. Indeed, some economists think the next slowdown could feed upon itself with fierce determination.

Canada and Mexico, which absorb nearly a third of U.S. exports, are a good example. With interest rates rising steeply as central banks defend their embattled currencies, both nations' appetite for American goods is almost certain to wane. If U.S. exports start to fade,

entire economy likely will follow. In turn will cool GDP in Europe and Asia, which rely on exports to the U.S. for a lot of their growth. "I've seen a period when it's so difficult to discriminate among markets," says Michael Wignall, chief global equity investment officer for G.T. Global Mutual Funds. "There's no place to hide."

NEWS BLUES. One result: In counter country, investors no longer willing to forgive economic excesses as readily as they did when U.S. interest rates were only 3%. That's especially true when they know they now earn 7.6% on two-year U.S. Treasuries. "That may not be the best yield available," says Salomon Brothers Inc. equity strategist David Shulman. "You know that at the end of two years the money will be there." Yields on emerging-market debt, meanwhile, have reached incredible heights. Morgan Stanley's Biggs notes that dollar-denominated Eurobonds issued by Cemex,

a fast-growing Mexican cement producer, have skyrocketed to 25% lately. Says Biggs: "I wonder how well emerging-market equities can do when the debt has such rich returns."

Amid heavy competition from bonds, equity traders seem intent on discounting the best of news as soon as it breaks. For example, traders hammered shares of both IBM and Compaq Computer Inc. after the computer makers announced excellent fourth-quarter profits. Traders figure profits have gotten about as good as they're likely to get any time soon.

It's much the same story in Japan, where the average price-earnings ratio of 76 reflected a strong belief that corporate profits would finally stage a healthy recovery this year. Then the Kobe earthquake struck, and analysts began tearing up earnings forecasts left and right. True, most expect profits and the economy to recover by 1996. But wor-

that as money tightens over the next six months, U.S. stock prices could retreat 15%. That, he adds, could spark "a further correction" in Europe.

TOUGH BATTLE. Declines in the industrial world are likely to cause new heartache for developing countries—even Asian ones with large pools of savings. Price-earnings ratios in these countries remain high by global standards and are thus vulnerable to further declines. Take Bombay. The average p-e ratio for major equities has fallen lately but is still hovering at 30—twice that for the U.S. "Investors will have to get used to lower p-e's," says Ashish Guha, head of investment banking at Bombay's Credit Capital Finance Corp.

One big reason: The collapse in Mexico has "increased risk premiums for the securities of all emerging-market economies," says Kemper Financial Services Inc. economist David D. Hale. With the easy money of the early 1990s

rapidly evaporating in Latin America, Asia, and other regions, these markets are now settling down for a long, tough battle for credibility that may take years to win.

The sorry situation of Teléfonos de México, perhaps the bellwether for all emerging-market stocks, illustrates how far a reputation can fall. After dropping 50%, to \$34, Telmex now trades at a mere seven times next year's estimated earnings. With profits still expected to grow by more than 20% annually in coming years, "that's completely stupid," says Oscar A. Castro, managing director of Montgomery Asset Management in San Francisco.

So is he buying? "A year from now, the equities no one wants to hold will again be the darlings of international investors," he predicts. However, "I will not fight the market," he says. And right now, the market is forecasting coming economic bad news.

By William Glasgall in New York and Bill Javetski in Paris, with Suzanne Woolley in New York and bureau reports

PUTTING THE BRAKES ON GROWTH



CHAIN REACTION Rising rates in Canada and Mexico could cool demand there for U.S. goods. If America's exports fade, its economy could follow—and trim growth in much of the world

ries over consumers and companies liquidating massive quantities of stocks to finance reconstruction are now weighing heavily over the Nikkei.

The result may not be pretty. After slumping 5%, to 17,885, on Jan. 23, the average could be set to fall 1,000 more points, says James Capel Pacific Ltd. strategist Jason James. But Japan isn't the only major market that could be in jeopardy. Smith Barney's Horne says

MEXICO

REMEMBER THOSE GUYS WHO BROUGHT YOU NAFTA?

The same lobbyists are storming the Hill to rescue the peso

It seemed like old times. On Jan. 23, lobbyists from 150 big U.S. companies packed a Capitol Hill room for a homecoming—and a pep rally. “You got us NAFTA. You won the GATT,” exhorted Representative Robert T. Matsui (D-Calif.), President Clinton’s chief Hill strategist in the North American Free Trade Agreement battle. “Now you can deliver on this one, too.”

Within hours, the old business coalition was up and running again. Their latest Mission Impossible: nailing down congressional passage of \$40 billion in loan guarantees to save Mexico from its current financial crisis. Corporate America’s message, as delivered by CSX Corp. Chairman John W. Snow, who is serving as peso point man for the Business Roundtable: Failure to approve the plan will mean “a drop in U.S. exports, increased illegal immigration, and a currency scare in the rest of Latin America.” And time is of the essence, Snow warns: If support for the guarantees unravels, the Mexican crash could get far worse.

With their mission clearly defined, the battle-tested NAFTA vets have swung into action. Plans for parachuting in former U.S. Presidents and dignitaries for photo ops were considered, then scrapped for lack of time. Instead, corporate honchos have dusted off the so-called White Book assembled by USA NAFTA, the pro-NAFTA lobbying group headed by AlliedSignal Inc. Chief Executive Lawrence A. Bossidy. The book is a district-by-district directory of major corporate employers with strong export ties to Mexico.

CORPORATE CATALOG. “We have a catalog now of who’s who in each district,” says one top corporate lobbyist. “Each company has a procedure in place to activate folks to do what has to be done.” Translation: Big corporate chieftains are at the ready to call their local representatives to voice support for the Mexican aid package.

Along with lawmakers representing export-dependent districts, the coalition is targeting legislators from border states to warn them that collapse of the

plan could trigger a flood of illegal immigrants. Hispanic business leaders have gotten behind the campaign, too, pledging to launch a letter-writing blitz in favor of the bailout. On Jan. 25, the Congressional Budget Office gave the business lobbyists more firepower: The CBO now estimates that the bailout package would be likely to generate a small profit for the U.S. government through Mexico’s payment of an upfront loan fee.

Meanwhile, Juan Gallardo, head of the powerful Mexican Business Coordinating Council, has set up in Washington to push for a deal. Among other tactics, the group will pressure U.S. suppliers to Mexican companies to support the bailout. Backers, however, have their work cut out for them. The aid package continues to meet fierce resistance from an anti-NAFTA coalition of unions, environmentalists, and American First conservatives. They view it as a risky bailout for a politically unstable and economically and environmentally irresponsible regime. The price they want for their support: stiff conditions that Mexicans would have a hard time swallowing. “Many critics are using this as an excuse to reopen NAFTA,” frets Varian Associates Inc. CEO Tracy O’Rourke, head of the National Association of Manufacturers. “If that happens, we lose the coalition.”

Playing the inside Hill game, moreover, won’t guarantee a win. The bailout

THE KNIGHTS OF NAFTA RIDE AGAIN

The pro-NAFTA coalition is now fighting for a Mexican bailout against too many odds—disapproval of the trade agreement.

THE PRO-BAILOUT POSITION

The Clinton Administration, led by Treasury Secretary Robert Rubin, wants to push through quickly \$40 billion in loan guarantees for Mexico. CSX chief John Snow and AlliedSignal Chairman Lawrence Bossidy are reassembling the business coalition that helped win the 1993 passage of the North American Free Trade Agreement. To ensure support, the Administration is willing to attach more conditions to the bailout.



SNOW



BOSSIDY



HELMS



PEROT

THE ARGUMENT AGAINST IT

NAFTA critics have been in full we-told-you-so fury since Mexico’s financial crisis knocked 39% off the peso’s value. Senate Foreign Relations Committee Chairman Jesse Helms (R-N.C.) vows “exhaustive and perhaps exhausting hearings” on a loan-guarantee package. He and America Firsters Pat Buchanan and Ross Perot are pushing for ironclad concessions from the Mexicans as a condition of aid. House Democrats who opposed NAFTA will demand other quid pro quos, such as guarantees of worker rights and stronger environmental standards south of the border.

s backers aren't sure that the 73 House Republicans who cam-
 med on promises to shrink govern-
 —let alone Democrats—will agree
 ore up a foreign government at
 ayer risk. "None of us wants to be
 position of being accused of funding
 out for Wall Street titans while
 e cutting benefits to widows and
 ans," says a senior Democratic aide.

Senate GOP conservatives, meanwhile,
 insist that Mexico create a currency
 board that would peg the peso's value
 to a strong currency. And in the House,
 Representative Barney Frank (D-Mass.),
 a NAFTA foe, is threatening a liberal walk-
 out without guarantees from the Mexi-
 cans of improved labor standards. "Let's
 see them pass it without us," he warns.
 Still, the Loan Rangers behind the

bailout are confident they'll have a plan
 on the President's desk by February.
 Administration officials are willing to
 attach some strings to financial support,
 preferably through nonbinding side let-
 ters. Backers reckon that with fears of a
 hemispheric financial panic offsetting
 other doubts, the ayes should have it.

*By Douglas Harbrecht and Dean
 Foust, with Amy Borrus, in Washington*

COMMENTARY

By Susan B. Garland

THE CRUX FOR CLINTON: FOLLOWING THROUGH

Is call for bipartisanship and a
 revival of community spirit
 sounded comforting. But beyond
 e warm and the fuzzy, Bill Clin-
 ton's Jan. 24 State of the Union ad-
 dress set the battle lines for fero-
 cious ideological combat with the
 republican-dominated Congress
 ver how much to shrink the federal
 government.

Feisty GOP lawmakers
 ink they have a mandate to
 ash and burn. That puts
 Clinton in a tough spot. He's
 ying to salvage an activist
 le for government at a time
 hen he and Washington are
 sliked and distrusted. To
 all it off—indeed, to save
 s Presidency—he has to
 nvince Americans that his
 policy isn't just another can
 Clinton Snake Oil.

WUNKY. The President's
 enormous credibility problem
 asks a reasonable vision of
 overnment—one that falls
 etween the extreme Demo-
 cratic view that government
 an solve all problems and
 e far-Right credo that the
 ds cause all problems. The
 unky name of his agenda,
 "New Covenant," lacks the
 arity of the GOP's "Contract
 ith America." But its mes-
 age, buried in the painfully
 ng address, is crisp: "We
 ould rely on government as
 partner to help us do more
 for ourselves."

This view of government as a
 iend rather than an overbearing
 arent was a major theme of Clin-
 ton's 1992 campaign, but he lost
 rack of it until forced to counter the
 epublicans' siren song. Although
 e GOP call for smaller govern-
 ment and lower taxes may reso-
 ate at first, Clinton is betting that

voters won't like the consequences.

Numerous polls bear him out. One
 conducted Jan. 4-8 for BUSINESS
 WEEK found that a majority oppose
 eliminating any specific government
 departments. Voters also like the
 idea of a balanced budget, but only if
 it means no cuts in Medicare or oth-
 er favorite programs. And a Jan. 19-

work. They don't want the Republi-
 cans to delete money for crime-pre-
 vention programs. And they prefer
 Clinton's welfare reform plan over
 the GOP proposal to cut off benefits
 with no job guarantees.

But even if Clinton has a more
 popular approach—will anyone be-
 lieve him? He didn't fulfill campaign
 pledges to enact middle-class
 tax relief, welfare reform, or
 campaign-finance reform
 when Democrats controlled
 Congress, so the public is
 wary of trusting him now.
 "He was right when he said
 the country is going through
 monumental changes, but is
 he the man to take us
 through them?" wonders
 Rutgers University political
 science professor Ross K.
 Baker.

GET CONCRETE. To reconnect
 with voters, Clinton must
 first quit the constant vacilla-
 tion. He needs to take a con-
 sistent point of view and
 show the backbone to fight
 for his agenda. Secondly, he
 should reframe the debate on
 his terms. His Reinventing
 Government initiative may
 be worthy, but the GOP will
 always outbid him on cutting
 government. The President
 must also show in concrete
 ways how GOP cuts would
 savage families. There will
 be plenty of evidence.

Finally, the President has to really
 believe his own message. Is there
 any soul behind the shtick? If this is
 just another political reinvention,
 Clinton-style, he won't stand a
 chance against the Republican on-
 slaught in Congress—or on the '96
 battlefield.

Garland covers the White House



NEW COVENANT "We should
 rely on government as a
 partner to help us do more for
 ourselves" — BILL CLINTON

22 Los Angeles Times poll found that
 while voters lean toward the Republi-
 cans on ideological grounds, they
 balk at many of the party's specific
 proposals.

For instance, they oppose GOP ef-
 forts to repeal the ban on assault
 weapons and to scrap Clinton's na-
 tional service program, which pays
 college tuition in return for volunteer

TRADE

AMERICA'S TRADE GAP: THE GOOD NEWS IN THE BAD NEWS

Its jump largely reflects growth and capital outlays



FIRST STOP, SEATTLE: The latest trade deficit breaks the record set back in 1987

The massive layoffs and restructuring that have wrenched Corporate America in recent years were supposed to have big payoffs. High productivity. Greater competitiveness in overseas markets. An America better able to defend its home markets. That's why the government's latest trade report, released on Jan. 19, came as such a shock.

It showed that last year's merchandise trade deficit, based on results through the first 11 months, is likely to hit \$170 billion. That would soundly top the previous record, in 1987, of \$160 billion—a number that fueled protectionist sentiment and led to tough trade legislation. Now, as another massive wave of imports rolls into the U.S., the question is: Has anything really changed?

Yes. Today's trade deficit is far different—and far less disturbing—than the tab the U.S. ran up in 1987. For one thing, today's economy is much larger, so the deficit now accounts for just 2.5% of gross domestic product, vs. 3.5% sev-

en years ago. Moreover, the rising deficit is due mainly to the success of the U.S. economy, which in 1994 grew almost twice as fast as the economies of its major trading partners. Faster growth translates directly into more imports, says William R. Cline, an economist at the Institute for International Economics, who estimates that each additional percentage point of economic growth raises the trade deficit by about \$15 billion.

Just as important, the surge of foreign products is far more concentrated in wealth-producing capital goods than in the past. This isn't just about sneakers and VCRs: The U.S. is importing more computers, machine tools, steel, and the like—products that are more likely to yield productivity gains for the U.S. economy. In 1987, 21% of imports were capital

goods. Now, they account for 28%. In the past year alone, imports of capital goods have increased some 21% (chart).

Indeed, import growth in recent years has been driven primarily by the U.S. investment boom. Purchases of foreign steel are up some 38% over the past year because domestic steelmakers haven't been able to meet demand from auto makers and other customers. "We're running as flat out as we can," says John R. Scheessele, president and CEO of WCI Steel Inc. In the machine tool industry, too, rising demand has boosted imports, generally without hurting domestic manufacturers. In the first 10 months of 1994, machine-tool imports totaled \$2.3 billion, up 30% from a year earlier—but domestic machine-tool orders are up about the same. "I don't hear anyone complaining about losing share to foreigners," says PaineWebber Inc. analyst Eli S. Lustgarten.

STRONG SUIT? Certainly, there are distressing sides to this record trade deficit—chiefly the flood of high-tech electronics from overseas. Over the past year, imports of semiconductors, computers, telecom equipment, and related gear rose by some 25%, or \$13 billion, a startling increase in an area that was supposed to be one of America's strong suits. Moreover, there are virtually no U.S. manufacturers supplying some of the hottest accessories, such as optical disk players in multimedia computers. In notebook computers, another fast-growing PC niche, as much as 40% of the materials cost for each computer resides in the screens—which are made almost entirely in Asia.

But this demand for foreign-made parts mainly reflects the explosion of computer and telecom equipment demand in the U.S.—which, again, should lead to higher economic growth. Consider personal-computer maker Dell Computer Corp. Some 65% to 70% of the parts going into its machines are produced outside the U.S., "and that proportion is increasing," says Stephen C. Martson, Dell's vice-president for worldwide procurement. "The labor cost for a lot of the things we

IMPORTS ARE FUELING INVESTMENT



*FIRST ELEVEN MONTHS COMPARED TO SAME PERIOD IN 1993
DATA: COMMERCE DEPT.

One worry: Many hot products with big futures, such as notebook screens, are made almost entirely overseas

...n't a lot, but it's significant enough
factories for our suppliers tend to
cated in Asia."

...en these difficulties in the high-
markets may not be so worrisome,
use those big import numbers may
rtificially skewed upward. Some
semiconductor manufacturers ship
is and other products overseas for
ng and assembly. When these prod-
come back into the country again,
are counted as imports. True, such
actions inflate exports, too—but
effect on imports likely is greater.

...ll the trade deficit begin shrinking
time soon? The growth gap be-
n the U.S. and its trading part-
should narrow in 1995, boosting
exports and restraining imports. In
ion, the weakening of the dollar
the past year against the yen and
mark will soon help, since exchange
take about two years to affect
e. And some industries are adding
city that should reduce import de-
d. North Star Steel Co. is spending
million on a new minimill in King-
Ariz., that will produce half a mil-
ions a year. And Oregon Steel Mills
is building a new mill in Portland
upgrading its rail mill in Colorado.
Chairman and CEO Thomas B.
und: "We'll be able to give the im-
s a run for their money."

CRAZY. On the downside, the U.S.
ll running massive trade gaps with
n and China that show no sign of
pearing. Imports of motor vehicles
parts surged some 15% over the
year, even though Japanese-trans-
production in the U.S. rose to
more than 2 million vehicles in '94.
nd the U.S. will be hurt in '95 by
weakness of its two closest trading
ners. Turmoil in Mexico will cut U.S.
rts to Mexico by some \$11 billion
'95, estimates DRI/McGraw-Hill. And
Canadian currency weakened by
20% against the U.S. dollar since
"it will be difficult for the U.S. to
ete with Canada," says Cline. In-
e, the trade deficit with Canada rose
\$3 billion in the first 11 months of
the third-largest deficit behind Ja-
and China. As a result, forecasters
as DRI/McGraw-Hill believe the
e deficit may actually grow in 1995.
at that in itself is not a bad sign for
economy. As the U.S. tries to re-
e itself for the Information Age,
old rule that developed countries
ld be capital exporters may no long-
old. Ultimately, the true test of a
e deficit is not how big it is but
wisely the U.S. uses what it buys.
y Michael J. Mandel in New York,
Gary McWilliams in Houston,
hen Baker in Pittsburgh, and
au reports

AUTOS

TOUGH TIMES FOR DETROIT? NO, JUST BAD DECISIONS

And Ford, the main culprit, should soon straighten itself out

Production cutbacks. Rising inven-
tories. Warnings from Chrysler
Corp.'s economist that more inter-
est-rate hikes could cripple auto sales.
Recent headlines from Detroit have
been unsettling. Is the industry driving
into a slowdown?

Maybe. More likely, though, Motown is
just grinding gears a bit, thanks to lousy
short-term decisions. Indeed, auto exec-
utives expect a better 1995 than '94—
once, that is, "we get through this bubble
of January and February," says Ford
Div. General Manager Ross Roberts.



FORD
AEROSTAR

Ford turned out so many Aerostar minivans that dealers balked at ordering higher-margin Windstars

Last year, U.S. car and light-truck
sales hit a vibrant 15.1 million. As 1995
began, though, some auto watchers be-
gan warning that sales would be hurt
by greedy pricing. For instance, by
eliminating the base version of its Lin-
coln Continental, Ford Motor Co. effec-
tively raised the model's price by \$7,000,
to \$41,375.

ROCKY START. But ill-thought marketing
and production strategies will likely take
more of the blame for 1995's rocky start.
Witness Ford's difficulties in small cars.
Sales of its subcompact Escort were
sideswiped by sweet lease deals Ford
offered in December to ensure that the
midsize Taurus would outsell Honda's
Accord. Buyers jumped at the chance to
lease a Taurus for \$259 a month, just
\$60 more than the Escort. "We're not
talking about a monumental jump in
payments to get a lot bigger car,"
says Jack A. Terhar Jr., president of

Sill-Terhar Ford in suburban Denver.

Trouble is, even as Escort sales dove,
Ford's factories kept churning them out.
Ford wanted a stockpile because it plans
to shut Escort plants this summer for a
model changeover. But Escort inven-
tories soared to 96 days worth at yearend,
and Ford recently had to cut production.
It doesn't expect the glut to be depleted
until the end of March.

Ford isn't the only company to make
miscues. In recent weeks, shoppers
searching lots for the \$9,500 version of
Chrysler's Neon came up empty: Trying

to boost margins, the
company made way
too many loaded-up
Neons selling for
\$12,000 or so. Belat-
edly, Chrysler offered
\$400 rebates to move
the metal while
boosting production
of the low-end Neons
consumers wanted.

Still, Ford seems
to be having the most
problems. Competi-
tion from the Taurus
also cut into Thun-
derbird and Contour
sales, prompting pro-
duction cuts for both.
The Contour suffered
from a recall and con-
sumers' unexpected

predilection for a \$14,665 version of the
car with a V-6 engine. Ford doesn't ex-
pect to be able to build all the V-6's it
needs until the fourth quarter.

Another example: Late last year,
Ford built up stocks of its Aerostar
vans, knowing production would suffer
in December and January when the
plant responsible for building the vans
also began making the Explorer. But
then dealers, who had loaded up on
Aerostars, balked at ordering the high-
margin Windstar. That idled the Wind-
star plant for at least a week.

When will auto sales pick up again?
Analysts expect the January numbers to
be depressed by a change in reporting
methods. But by the time the first quar-
ter is over, Ford and Chrysler should be
back on track—and the great auto-sales
slump of 1995 could be winding down.

By James B. Treece, with David
Woodruff, in Detroit

CORPORATE PROFITS

A BARN BURNER OF A FOURTH QUARTER

But the stellar performance is still leaving Wall Street cold

The early word on the fourth quarter: another blowout. Earnings rose an average 46% on a revenue hike of 10% for the 83 companies in BUSINESS WEEK's flash report. But Wall Street is unimpressed. Case in point: Compaq, which had a 61% jump in profits. "We believe we'll see continued good growth in the U.S., a more optimistic pattern emerging in Europe, and very strong growth in [Asia]," says CEO Eckhard Pfeiffer. But Compaq shares fell 12% on fears of slowing growth.



CORPORATE PROFITS

A NEW LIFE FOR CAT?

The UAW and management seem ready to talk turkey

When is good news not good enough? Ask Caterpillar Inc. On Jan. 19, the construction-equipment giant announced that both sales and profits hit record levels in 1994. Net income climbed to \$955 million, up

from \$345 million before extraordinary items in 1993, on sales of \$14.3 billion, a 23% increase. But Caterpillar's stock plunged 6.6% that day, to 54%. Why? Its fourth-quarter gross profit margin was 22.4%, no higher than 1993's fourth quarter. And that spooked Wall Street.

Maybe the Street should be looking forward, not backward. On Jan. 31, Caterpillar and the United Auto Workers will restart contract negotiations with the help of the Federal Mediation & Conciliation Service. And after months of standoff, brought on by management's firing of union members, the company and the UAW appear ready to talk turkey. "This is the first serious ef-

fort by both sides," says a source close to the negotiations.

The seven-month dispute has hurt Cat—but not by much. The company says defecting strikers, plus its use of management employees, new hires, and temporary workers, helped it raise production 14% higher in the second half of 1994 than in the first. Still, more than 9,000 of its UAW-represented workers remain on strike. And the hiring and training of temps, plus higher sales of low-margin products, shaved \$30 million to \$40 million off Cat's operating income last year, figures Smith Barney Inc. analyst Tobias M. Levkovich.

Now, exhaustion may be pushing both

CURRENT QTR. SALES
(MILLIONS)

INDUSTRIALS	196,236.0
ABBOTT LABORATORIES	2,481.0
ALCOA	2,641.0
AMERICAN BRANDS	3,750.0
AMERICAN HOME PRODUCTS	2,585.0
AMOCO	6,952.0
BAUSCH & LOMB	479.0
BOEING	5,120.0
BRISTOL-MYERS SQUIBB	3,247.0
CATERPILLAR	3,928.0
CHAMPION INTERNATIONAL	1,465.0
CHEVRON	8,035.0
CHRYSLER	14,260.0
CORNING	1,280.0
DUPONT	10,429.0
EXXON	30,561.0
GENERAL ELECTRIC	17,791.0
INLAND STEEL INDUSTRIES	1,156.0
JOHNSON & JOHNSON	4,090.0
KELLOGG	1,592.0
KIMBERLY-CLARK	1,920.0
MARTIN MARIETTA	2,785.0
MCDONNELL DOUGLAS	3,512.0
MERCK	3,871.0
MINNESOTA MINING & MFG.	3,855.0
MOBIL	18,892.0
MONSANTO	2,090.0
PACCAR	1,113.0
PHILIP MORRIS	16,501.0
PPG INDUSTRIES	1,659.0
REYNOLDS METALS	1,684.0
TELEDYNE	644.0
TEXACO	8,959.0
TRW	2,446.0
WARNER-LAMBERT	1,720.0
WEYERHAEUSER	2,733.0
SERVICES	31,197.0
AMERICAN EXPRESS	3,802.0
AMR	3,995.0
BANKAMERICA	NA
BANKERS TRUST NEW YORK	NA
BEAR STEARNS†	826.0
BURLINGTON NORTHERN	1,344.0
CHASE MANHATTAN	NA
CHEMICAL BANKING	NA

CHG.	EST. EPS (11/23)	REPORTED EPS	DIFF.		CURRENT QTR. SALES (MILLIONS)	% CHG.	QTR. PROFITS (MILLIONS)	% CHG.	EST. EPS (11/23)	REPORTED EPS	DIFF.
-56	0.93	1.01	+0.08	CITICORP	NA	NA	1,042.0	+81	1.41	2.20	+0.79
+8	0.53	0.53	—	CSX	2,540.0	+10	239.0	+58	1.90	1.89*	-0.01
NM	0.72	0.75*	+0.03	HILTON HOTELS	405.3	+10	38.1	+18	0.67	0.79	+0.12
228	0.93	1.02*	+0.09	MERRILL LYNCH	4,483.8	-1	161.6	-53	1.29	0.76	-0.53
+4	1.29	1.30	+0.01	MORGAN (J.P.)	NA	NA	193.0	-51	1.67	0.96	-0.71
-8	1.01	1.08	+0.07	NATIONSBANK	NA	NA	405.0	+9	1.57	1.45	-0.12
NM	0.73	-1.05	-1.78	NORTHWEST AIRLINES	2,192.0	+2	35.9	-242	0.11	0.23	+0.12
-48	0.37	0.46	+0.09	ROADWAY SERVICES	1,526.6	+11	13.7	-68	0.77	0.35	-0.42
-61	1.15	1.15*	—	SCHWAB (CHARLES)	270.4	+5	33.8	+19	0.56	0.58	+0.02
89	1.18	1.38	+0.20	TRAVELERS	4,380.7	+103	333.5	+12	1.02	0.99	-0.03
NM	0.42	1.02	+0.60	UAL	3,439.0	+3	11.0	NM	-0.68	-0.98	-0.30
79	0.80	0.81	+0.01	UNION PACIFIC	1,992.0	+4	235.0	0	1.12	1.14	+0.02
50	2.51	3.20	+0.69	WELLS FARGO	NA	NA	216.0	+14	3.95	3.96	+0.01
NM	0.49	0.14	-0.35	TECHNOLOGY	43,957.2	-14	3,432.0	+53	0.98	1.09	+0.11
173	0.84	0.95	+0.11	ADVANCED MICRO DEVICES	545.2	+32	40.8	-2	0.76	0.39	-0.37
+27	1.08	1.53	+0.45	APPLE COMPUTER††	2,832.0	+15	188.0	+370	1.04	1.55	+0.51
+18	0.99	0.99	—	COMPAQ COMPUTER	3,251.0	+48	243.0	+61	0.93	0.90	-0.03
NM	0.67	0.66	-0.01	CONNER PERIPHERALS	591.6	+3	44.2	+423	0.28	0.84	+0.56
+13	0.59	0.59	—	GENENTECH	207.8	+29	18.6	0	0.24	0.15	-0.09
+3	0.71	0.70	-0.01	HONEYWELL	1,737.7	+7	104.9	-7	0.82	0.81	-0.01
-25	0.86	0.66	-0.20	IBM	19,897.0	+3	1,230.0	+222	1.70	2.06	+0.36
+18	1.12	1.30	+0.18	INTEL	3,228.0	+35	372.0	-37	1.57	1.56*	-0.01
NM	1.35	1.39	+0.04	LOTUS DEVELOPMENT	264.5	-5	14.4	-51	0.45	0.30	-0.15
+15	0.61	0.61	—	MICROSOFT†	1,482.0	+31	373.0	+29	0.56	0.60	+0.04
+16	0.79	0.79	—	MOTOROLA	6,453.0	+29	515.0	+51	0.70	0.86	+0.16
50	1.41	1.28	-0.13	RAYTHEON	2,729.0	+8	205.7	+11	1.59	1.61	+0.02
-7	0.54	0.51	-0.03	SILICON GRAPHICS†	524.0	+41	53.9	+48	0.31	0.34	+0.03
+25	1.40	1.47	+0.07	SYBASE	214.4	+56	28.5	+60	0.49	0.52	+0.03
222	1.26	1.27	+0.01	UTILITIES & TELECOM	53,311.8	+6	4,638.2	+84	0.69	0.69	—
180	0.67	0.72	+0.05	AMERICAN ELECTRIC POWER	1,283.0	-4	117.6	-26	0.77	0.56	-0.21
NM	0.36	0.71*	+0.35	AMERITECH	3,181.2	+5	429.1	-8	0.76	0.78	+0.02
+4	0.42	0.30	-0.12	AT&T	21,110.0	+11	1,338.0	+72	0.89	0.85	-0.04
+9	0.95	1.42	+0.47	BELL ATLANTIC	3,486.5	+4	314.9	-7	0.81	0.72	-0.09
58	1.38	1.49	+0.11	BELLSOUTH	4,394.6	+7	558.5	NM	1.04	1.12	+0.08
NM	1.01	1.02	+0.01	NYNEX	3,390.9	0	198.3	-25	0.80	0.80*	—
86	0.81	0.91	+0.10	PACIFIC GAS & ELECTRIC	2,638.2	-3	103.5	-50	0.46	0.21	-0.25
+2	1.21	1.26	+0.05	PACIFIC TELESIS GROUP	2,356.0	+3	262.0	NM	0.64	0.62	-0.02
+15	0.67	0.65	-0.02	PUBLIC SERVICE ENT. GROUP	1,468.1	0	142.0	+71	0.51	0.54	+0.03
NM	0.19	0.59*	+0.40	SBC COMMUNICATIONS	3,207.6	+11	424.7	+10	0.74	0.71	-0.03
+19	1.41	1.41	—	SCECORP	2,041.7	+11	143.6	-3	0.30	0.30	—
-64	2.21	1.19	-1.02	SOUTHERN	1,915.0	-2	197.0	+26	0.23	0.27	+0.04
-76	0.38	0.22	-0.16	U S WEST	2,839.0	+6	409.0	+55	0.69	0.89	+0.20
+20	1.43	1.51	+0.08								
-27	1.33	1.10	-0.23								
-48	1.40	1.24*	-0.16								

† Second-quarter results †† First-quarter results NM = not meaningful NA = not available *EPS adjusted for special items
 DATA: STANDARD & POOR'S COMPUSTAT, A DIVISION OF MCGRAW-HILL INC. EARNINGS ESTIMATE DATA PROVIDED BY I/B/E/S INTERNATIONAL INC.,
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to the table. Caterpillar has the
 hand, having proved it can build
 without the union. But, accord-
 to an employee at one Caterpillar
 y, 2 in 10 temporary workers hired
 the strike have left or been dis-
 d. If true, that means
 faces the cost of con-
 y training and integrat-
 ew workers. The com-
 says turnover among
 is not a problem.
OLDENED. The union is
 even greater pressure.
 y day, some 5,200 of its
 bers cross the picket
 including 1,100 hired in

part to replace retirees since the strike
 began in late June. And Cat rival Deere
 & Co. has been emboldened to resist
 the union's demands. UAW members at
 Deere have worked without a contract
 since last fall.

Few expect there will be a swift end
 to the Cat conflict, though. A compa-
 ny-imposed contract has been in effect
 since April, 1992, and the UAW wants
 to win some concessions before mem-
 bers head back. But most observers ex-

pect Cat to offer only to
 raise retirement benefits or
 improve job security a bit.
 Working out the details
 could take at least two
 months, say company and
 union sources. Till then,
 Cat's gross margins may suf-
 fer—along with the striking
 workers.

By Kevin Kelly in Chicago



OUT IN THE COLD
 The UAW still has
 some 9,000 workers
 on strike, but many
 have crossed the
 picket lines, and
 output at Caterpillar
 has not fallen off



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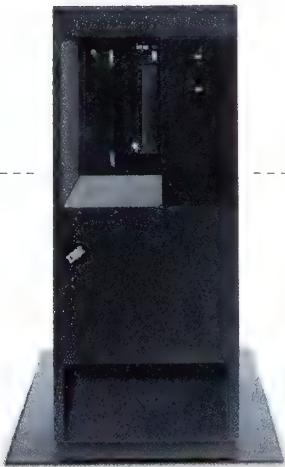
(If you're saving less, it isn't AS/400)

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CELEBRITIES

THE WALL STREET WAG COMPANIES LOVE TO HATE

Subjects of Dan Dorfman's reports threaten lawsuits—or worse

Dan Dorfman is used to suffering his share of barbs: When you make a living dishing Wall Street dirt, criticism comes with the territory. But death threats? After his Jan. 20 CNBC television report mentioned an alleged Securities & Exchange Commission investigation into Hanover Sterling, a small New York brokerage, one caller advised Dorfman that he needed "police protection." Another, Dorfman says, warned: "If you talk about us again, we're going to kill you." "This," Dorfman says, "was just an unusual day."

It has been that sort of month, though. More and more, the targets of Dorfman's reports are fighting back, denouncing a swash-buckling style they say is heavy on rumor and light on fact-checking. Coca-Cola Co., Caremark International, and others have publicly decried Dorfman's prognostications and challenged his sourcing. Hanover Sterling notes that the SEC investigation is more than a year old and says it has done no wrong. Says Adolph J. Ferro, CEO of Epitope Inc., a small biotech company that is considering suing Dorfman over reports about its AIDS test: "I have no idea where he comes up with the [sources] he comes up with."

LONG REACH. Dorfman, a 63-year-old veteran of the market rumor mill, airs his reports five times a day on CNBC and writes a monthly column for *Money* magazine. For this, he makes what industry sources estimate at \$600,000 a year. CNBC says it stands behind its star. But his TV reports, broadcast to some 500,000 viewers while the markets are open, often move stocks dramatically, producing millions of dollars in gains or losses.

Case in point: a Jan. 13 report that Coca-Cola Co. might be set to launch a hostile \$60-a-share bid for Quaker Oats

Co., maker of Gatorade. Relaying a rumor he says he had heard three times in two weeks, Dorfman claimed in a CNBC broadcast that the cola giant had received approval for the raid from its largest shareholder, Warren E. Buffett. Coke, Quaker, and Buffett all refused to comment to him.

Coca-Cola stock immediately dropped



“Why did Coke personalize it? Because I can move a market? What has that got to do with anything?” —DAN DORFMAN

after the report, on a day when the broader market gained sharply. Coke was not pleased. Abandoning its usual corporate decorum, it responded in a statement with this zinger: "Dan Dorfman does not have a clue."

Ouch. "Why did Coke personalize it?" Dorfman laments. "Because I can move a market? What has that got to do with anything?" Coke won't elaborate. But

its attack seemed to bring other criticism out of the woodwork. Caremark, for instance, issued a statement on Jan. 13 denying a Dorfman report that it would use proceeds from the sale of its home infusion business to pay a forthcoming criminal settlement with the federal government. In fact, no settlement has been reached—and in any case, the company has repeatedly said it will use the money to fund other operations.

PIGGYBACK SQUEALS? More complaints followed—not all of them fully credible. Incomnet, a Woodland Hills (Calif.) long distance service reseller, loudly denied Jan. 17 Dorfman report that the company was a target of a new SEC investigation of alleged unfair and unethical sales practices. "Categorically false," said Incomnet. But the company is being investigated, and it qualified its response to that effect in two subsequent press releases. Yet CEO Sam D. Schwartz still argues that Dorfman overstated the scope of the inquiry. Dorfman maintains Incomnet's admission proved him right.

In November, Atari Corp. publicly criticized Dorfman's reliance on short-seller Martin D. Sass for a negative story on the company. An Epitope may sue Dorfman for his reports on its new AIDS test. On Mar. 21, 1994, Dorfman said the test stood only a 1% chance of Food & Drug Administration approval. The FDA sent Epitope a letter saying the report was untrue, and on Dec. 23, the product was approved.

Epitope has already settled a suit against A. Kipke, a former Kidder, Peabody & Co. broker, alleging false and misleading statements. Kipke admitted he planted inaccurate stories about Epitope while selling the stock short. He was also a regular source for Dorfman. Says Dorfman: "I can be sure that everyone speak to is 1,000% ethical."

Dorfman says he's just an earnest reporter doing his job. "I don't recommend stocks. Don't ask me to be an investment adviser," he rails. But to many viewers, he is just that—and that's what has so many companies so upset.

By Maria Mallory in Atlanta, with Mark Landler in New York and bureau reports

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TELEVISION

THIS BELL ISN'T RINGING

Who will buy PBS? Not Bell Atlantic—despite the hype

Bell Atlantic's bid to buy PBS is a long shot, though based across town, the phone company's interest in the station is well known. But Bell Atlantic's chief executive, Raymond W. Smith, says the company's interest in PBS is "a pretty far-fetched notion."

Yet Bell Atlantic has become the corporate poster child for the debate over privatization of public broadcasting. On Jan. 22, Senate Commerce Committee Chairman J. Bennett Johnston, R-S.D., after meeting with CEO Raymond Smith and other BA execs, casually let drop on CBS News' *Face the Nation* that Bell Atlantic was "seriously considering

to buy public stations or programming.

Not exactly, says Bell Atlantic. It hasn't explored the idea, doesn't have any concrete plans, and isn't mulling any offers, spokesmen say. The company has been unwilling to sponsor a series for \$5 million, a fraction of the \$300 million that Washington spends yearly to subsidize public broadcasting.

But the story is running way ahead of reality. The company's interest in PBS was first reported in a story that popped. Some phone company watchers say Pressler wanted to attach a big-company name to his idea, and Bell Atlantic always is prone to be snipped because it will need support when Congress crafts telecommunications laws in coming months. Bell Atlantic denies any such quid pro quo.

Certainly, the phone giant needs TV programming such as *60 Minutes*, starring Barbara Walters, to fuel both its nascent cable

system in New Jersey and the interactive video service it plans to offer by 2000. But owning stations would compete with its own cable delivery system. And few of the nation's 350 public-TV stations, in any case, likely would want to be acquired. Going commercial "would defeat the purpose of this industry," says Al

BAD FIT? BELL ATLANTIC CHIEF SMITH



thur Albrecht, general manager of WVPB in Harrisburg, Va. Ervin S. Dugan, CEO of the Public Broadcasting Service, says

that privatization could "kill the enterprise. For all the bombast

there is one near-certainty: Public TV likely will lose some funding. And while many in Washington see privatization as unlikely, Pressler's tactics have drawn one interested party. Jones Intercoable Inc. in Colorado Springs may yet find home in the private sector.

By Joseph Weber in

TECHNOLOGY

A PACKAGE FOR EVERY PERSON

Indigo's new printing system can do short, custom runs

Imagine the sales boost Coca-Cola Co. could get if it printed full-color pictures of coach Joe Paterno on every can of Coke at Penn State foot-

ball season. Some major printers are clamoring for the first machines. Toronto-based Moore Corp., the giant maker of business forms, plans to produce customized labels with its machine. Says Moore Chief Executive Reto Braun: "This is a breakthrough. It's one more strong indication that chip technology is entering the printing business."

TILES AND TABLECLOTHS. Omnius does away with the bulky, awkward metal printing plates used in conventional offset presses. In its process, ink is laid directly onto a smooth, rubbery roller by computer, then transferred onto the print surface. The ink is specially formulated to lift cleanly off the roller, so a different image can be printed in

each revolution. The technology is the same as in the E-Print process, which allows for

successful last year. But E-Print can print only on single sheets of paper. Omnius can handle rolls of paper, plastic, film, or cardboard, as well as cans, bottles, and ceramic tiles.

Where will the new technology lead? Landa foresees beer cans customized for weddings and full-color product brochures that can be changed weekly, to say nothing of coordinated kitchen tiles, curtains, and tablecloths, all printed overnight on an Omnius machine. The one drawback: Indigo's special ink is more expensive. So for long runs—say, 100,000 or more, depending on the type of job—it still makes sense to gear up a conventional press. Landa vows to refine Omnius for bigger jobs.

Omnus looks like another big win for the Canadian-born Landa, 48, who became one of Israel's richest men last May when his company went public in the U.S. with a market value of \$1 billion. Landa's family trust retains 70% of Indigo's shares. The stock sagged last summer but has since rebounded—and surpassed the offering price the day Omnius was announced. If Omnius takes off the way early customers predict, the main thing it will be printing is money.

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event? That kind of customized packaging is a market Indigo is targeting. "We're going to prepare a combination of short and long runs," says Landa. He claims his new Omnius machine, announced in Jan. 17, makes it possible to print on a wide variety of materials, including glass and paper packaging in

By Joseph Weber in

ED BY KEITH H. HAMMONDS

CLOSER LOOK BAUSCH & LOMB

BUSCH & LOMB, ADMITTING appropriately recorded and profits in late 1993, on Jan. 25 its accounting practices were being investigated by the SEC. The statement followed a Dec. 19 BUSINESS WEEK article questioning the way B&L booked sales and profits from an unusually large shipment of contact lenses to distributors in the final days of 1993. Many distributors, threatened with loss of B&L business unless they accepted the lenses, say they were promised they wouldn't have to pay for the lenses until they were sold.

CLOSING BELL

MERRILL'S MESS

Sins of Orange County haven't yet been visited on Merrill Lynch—but the brokerage had a disappointing fourth quarter anyway. Profits fell 53%, to \$162 million, on weakness across Merrill's businesses. Worse could come if Merrill has to use reserves for losses in Orange County, Calif., which, citing Merrill's role in the derivatives debacle, is suing for \$2 billion. Even on Jan. 25, Merrill named as its President David Komansky, the executive ultimately responsible for the firm's Orange County dealings.

MERRILL LYNCH STOCK PRICE



MAY 6, '94 JAN. 25, '95
DATA: BLOOMBERG FINANCIAL MARKETS

Accounting experts quoted by BUSINESS WEEK said that such shipments should not have been recorded as sales. According to B&L, the yearend shipments resulted in a \$10 million net profit. B&L, which in December denounced the BUSINESS WEEK story as "false" and "ridiculous," now admits some bookings were inappropriate, but believes they were not material to 1993 results.

BREAKING THE BOND WITH FIDELITY

AFTER A YEAR OF FLAT-OUT bad results, Fidelity Investment's top bond executive is resigning. Thomas Steffanci will step down on Feb. 28 as head of Fidelity's bond mutual funds, in part because of disagreements with investment chief Gary Burkhead, sources say. Burkhead stepped up his supervision of bond funds last year, pressing managers to make more conservative investments. No wonder: After losing bets on Latin American debt, derivatives, and long-term bonds, the firm's bond assets shrank 11%, to \$24 billion, last year. Steffanci said his decision to leave was "purely personal."

THE HIGH COURT CRIES AGE BIAS

CHRISTINE MCKENNON, 62, AN ex-secretary, got relief at the Supreme Court, which on Jan. 23 backed her age-bias suit against Nashville Banner Publishing. The court decided the company could not bar McKennon—whose job went to a younger woman—from collecting back wages on the basis of evidence that she had stolen confidential files. Antibias advocates applauded the decision but remain concerned that the high court may not be as sympathetic in other pending civil rights cases this term involving

HEADLINER: STANLEY SPORKIN

A HARD-LINE JUDGE FOR MICROSOFT?

Federal Judge Stanley Sporkin has managed to unnerve both Microsoft and a host of U.S. government officials. At a lively court hearing on Jan. 20, the Washington jurist made it clear he would not automatically sign off on the two parties' proposed anti-trust settlement of last July without probing the accord. "I don't want to be made a fool," he said.

The former Securities & Exchange Commission enforcement director didn't let either top Justice Dept. trustbuster Anne Bingaman or Microsoft's lawyers off the hook. While he's no

cybernaut—he learned to use his PC just three years ago to play computer chess—he questioned why certain alleged Microsoft practices

weren't covered by the government's case. The consent decree, he said, "doesn't go far enough."

Bingaman defended her right as prosecutor to decide which charges to bring. "You can't force me to file a case," she said, pounding the table. Want to bet? The feds and Microsoft now await a ruling that could either end the case or lead to more legal battles.

By Catherine Yang



ing federal minority-contracting programs, school desegregation, and voting rights.

THE VIDEO-DISK WARS HEAT UP

TIME WARNER AND TOSHIBA have come up with a digital video disk that may do in the Sony-Philips rival. On Jan. 25, the two lined up eight of the world's biggest electronics and showbiz companies to back its system of encoding movies on familiar five-inch silvery compact disks. Sony said it would study the rival system—leaving room for retreat. That's sensible. Unless there's a compromise, both camps will have incompatible \$500 players on the market by yearend.

CLEAT ME IN ST. LOUIS

"IT WAS EITHER FOOTBALL OR tractor pulls," says former

U.S. Senator Thomas Eagleton (D-Mo.). Um, we'll take the pigskin. Eagleton led a drive that now appears likely to bring professional football's Los Angeles Rams to St. Louis. The city, desperate to fill its new 70,000-seat, \$260 million stadium, will give the Rams' owners virtually all stadium revenue and guarantee sales for 15 years of luxury boxes and club seats. That will lift the team's pretax profits by \$20 million a year.

ET CETERA...

- The SEC is investigating claims of insider trading and other abuses at Greyhound.
- Irwin Jacobs charged KnowledgeWare Chairman Fran Tarkenton with fraud.
- Lotus cut prices on Notes, its hottest software item, then revealed poor earnings.
- Coffee break: A customer sued Starbucks after spilling java from an "unsafe" cup.

"Mosam" has some great stories about the Chesapeake Bay.

If you want to know how to build a Deadrise workboat, or how the crabs are running, or even about the muskrat population 40 years ago, all you have to do is spend a few minutes with Elmer "Mosam" Ford.

"Mosam" knows all the stories. And if he embellishes them a little, well, that makes them all the better.

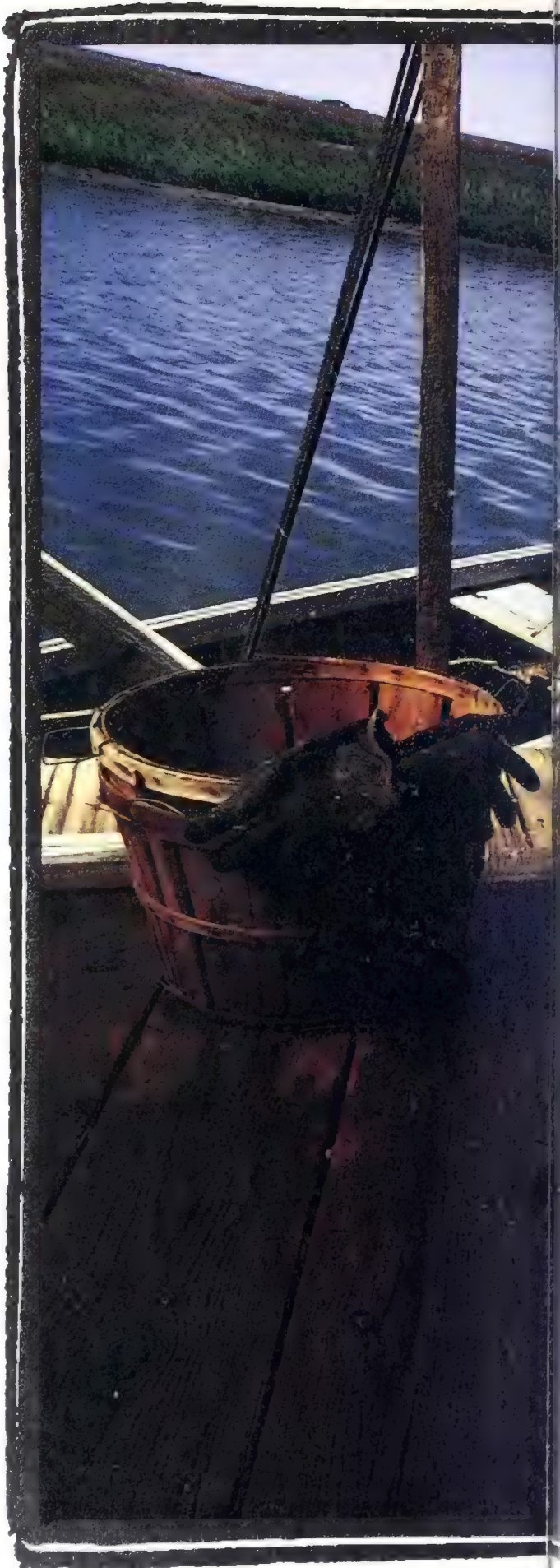
The U.S. Environmental Protection Agency also has some things to say about the Bay. And while these stories are more serious than "Mosam's," they need to be told, too.

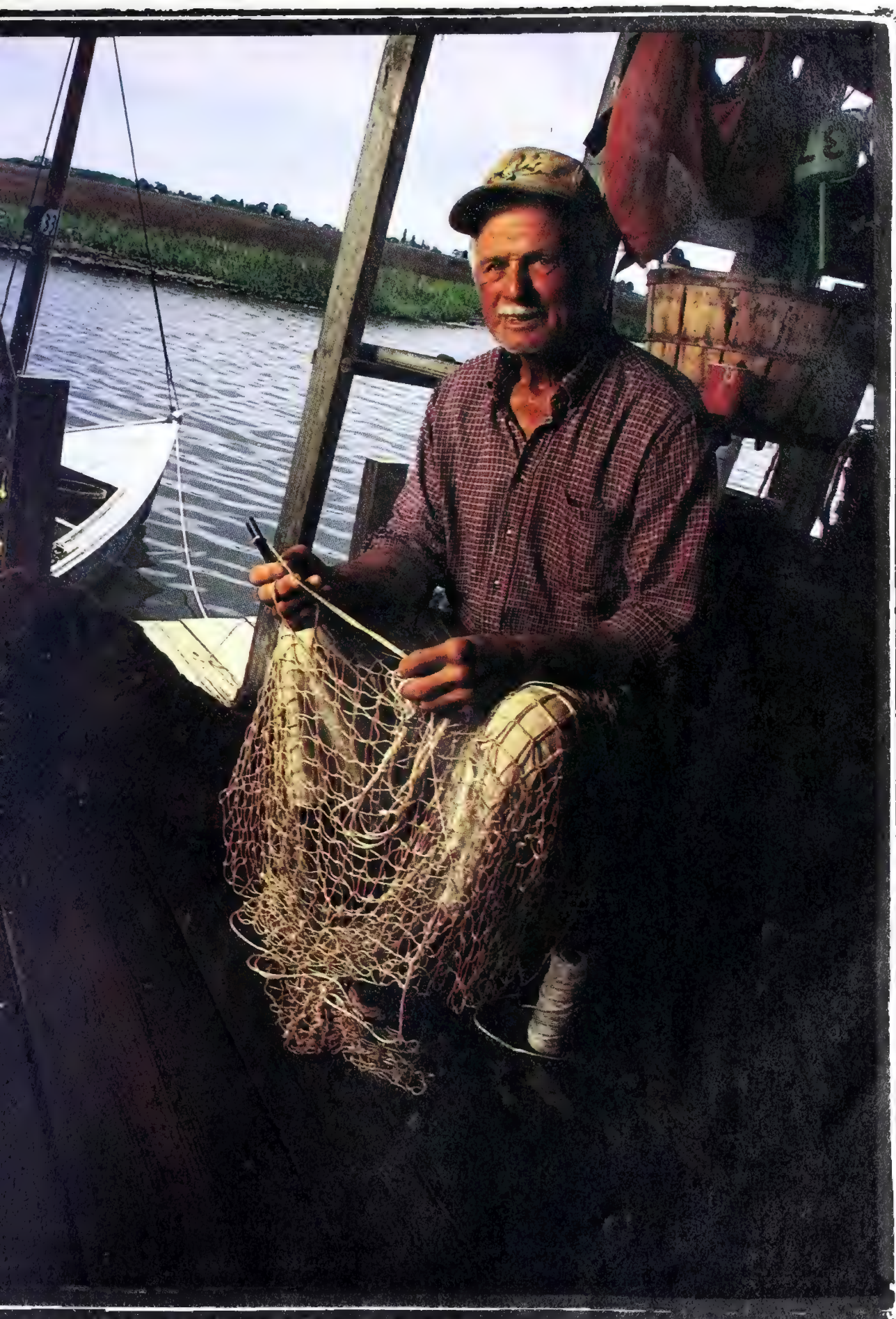
The stories use computer models and simulations to predict the effects of human interaction with the Bay. They help EPA decision-makers determine how to protect this national treasure from chemical and toxic pollutants. The same techniques are also being applied to safeguard other precious national resources.

It takes a lot of teamwork to keep the environment clean. Martin Marietta is proud to help by processing vital information for the EPA using the most sophisticated computing resources available. Together, we all can help keep America beautiful.

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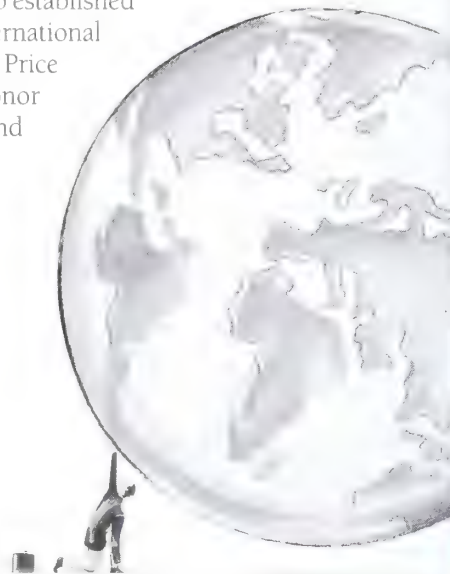
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EDITED BY OWEN ULLMANN

THE PLAYERS CHANGE, BUT GRIDLOCK IS STILL THE NAME OF THE GAME

To see what's wrong with the new Congress, look no further than the unfunded mandates reform bill now bogged down on both sides of the Capitol. The measure bars Washington from forcing states and cities to comply with federal regulations, from clean air to voter registration, unless funds foot the bill. Passage should have been a snap. It's a priority of Republican congressional leaders. President Clinton backs it. And a bipartisan coalition of public officials says the country has pleaded for it.

Why is it languishing? Because politics-as-usual survived the election earthquake of November—only the roles have been reversed. A GOP majority bent on exerting control is ignoring opposition amendments, however worrisome. And the Democratic minority is adopting guerrilla delay-and-block tactics honed over the years by the GOP.

WARRING. Although the bill will pass, the top sends a sharp warning to House Speaker Newt Gingrich and his Republican revolutionaries: If modest initiatives can get snarled by partisan bickering, imagine the fate that awaits radical changes such as welfare reform, regulatory relief, and spending cuts. The fight over unfunded mandates was triggered by a GOP miscalculation. In their zeal to pass the measure before Clinton's State of the Union address on Jan. 24, party leaders rushed it to the House and Senate floors without taking normal precautions to iron out kinks in committee. Sure enough, Democrats found a way to block it. The bill could unintentionally penalize private enterprise. It exempts governments—but not businesses—from the costs of new health, safety, and environmental rules. It creates a competitive disadvantage for companies bidding against localities in a growing market for privatizing government services. Private trash haulers would have to implement the latest waste regulations at their own expense, but

competing municipal sanitation departments would be subsidized by the feds. "This will have an unfair and burdensome impact on business," protests Senator Joseph I. Lieberman (D-Conn.), a probusiness moderate who has supported unfunded-mandate curbs in the past. Handed a chance to tarnish the GOP's business-friendly image, Lieberman and Senator Carl Levin (D-Mich.) pounced. They sought to curtail exemptions for localities in fields where they compete with the private sector. But a united GOP blocked the move, 53-44. "They view this as a test of their political manhood," gripes a Democratic strategist.



BUSINESS' PAL? Lieberman

OVERSTATED? The GOP's rush worries some business lobbyists. "We'd like to be assured that we do not have a competitive disadvantage with the public sector over the long term," says Kevin Stickney, vice-president of Wheelabrator Technologies Inc., a New Hampshire environmental technology company. But Republicans say business concerns may be overstated. Senator Dirk Kempthorne (R-Idaho), for one, promises to seek a remedy if any discrimination against the private sector occurs.

The GOP charges that the Democrats' real aim is not to aid business but to kill the bill. And they have a point. While Lieberman and Levin seem sincere about correcting the Republicans' hasty move, others want to embarrass the new GOP rulers by gumming up Congress' machinery. Senator Robert C. Byrd (D-W. Va.), a master parliamentarian, single-handedly caused a five-day delay in passage of a bill forcing Congress to live under laws it applies to business, and now he's at it again on unfunded mandates. Senate Majority Leader Bob Dole refers to his tactics as "Byrdlock."

But for Democrats, Byrdlock is just a variation of the old game voters thought they were ending last November. It's known as Gridlock, and the players show no signs of tiring.

By Richard S. Dunham

CAPITAL WRAPUP

NEW BROWN: BACK IN THE SOUP

For the first time, Commerce Dept. leaders are sweating over Republicans' delving into Secretary Ronald H. Brown's tangled personal finances. They fear a protracted investigation into his past business dealings will embarrass President Clinton and cloud Brown's future. "We're in trouble," frets one aide.

On Jan. 24, 14 GOP senators asked the Justice Dept. to look into whether Brown filed inaccurate financial statements or avoided taxes in 1993. The

request came after a House committee linked Brown financially to Corridor Broadcasting Corp., a Washington company that defaulted on \$47 million in debt to the Federal Deposit Insurance Corp. and Resolution Trust Corp. from '91 through '93. The FDIC said on Jan. 25 that its inspector general will investigate the matter. Brown's attorney, Reid Weingarten, calls the charges "hypertechnical."

The Commerce chief's supporters lament that Brown, cleared of an earlier charge of taking a \$700,000 bribe from a Vietnamese businessman, brought

the new GOP inquiry on himself by stubbornly refusing for two years to disclose even innocent details about his complicated business affairs. Aides say his problems have been compounded by Commerce ethics officer Barbara S. Fredericks, who angered Republicans in the last Congress with her staunch defense of Brown's right to shield most of his dealings from scrutiny. Even Democrats have been aghast at Brown's lack of disclosure. "It's pay-back time," sighs a top Democratic congressional aide.

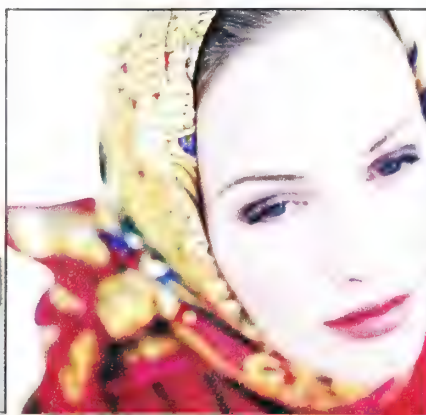
By Douglas Harbrecht

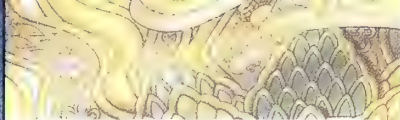


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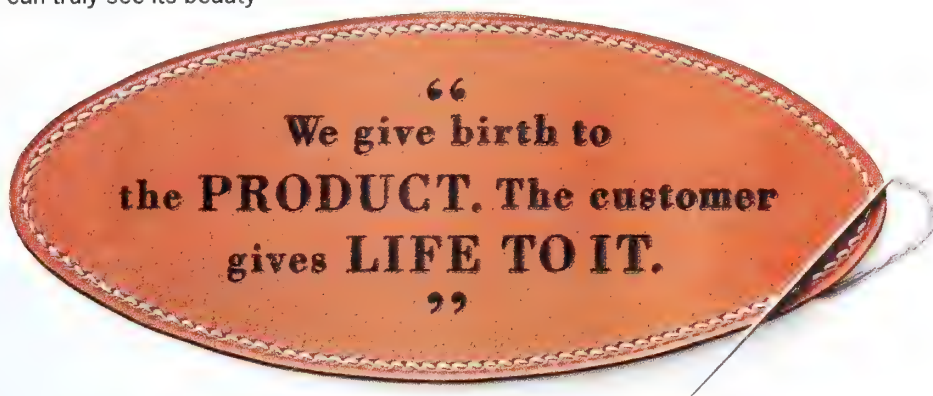




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CHINA

WILL POWER STRUGGLE SPELL PARALYSIS?

Deng's passing will leave a leadership unsure of how—or whether—to pursue reform

For each of the past seven years, Deng Xiaoping has headed for the Xi Jiao Guest House in Shanghai to celebrate the lunar New Year. This year, the 90-year-old leader is breaking with tradition. Even though Shanghai is experiencing its warmest winter on record, Deng remains in Beijing so hobbled by health problems, including kidney failure, that many wonder whether his doctors will be able to keep him alive for long. "The situation is deteriorating by the week," says one well-connected Chinese economist.

Whenever it comes, Deng's long-awaited departure will create a huge void in a political system where he has called the shots from behind the scenes for years. A power struggle is already quietly under way as various factions jockey for control. The leadership is likely to present a unified front at first, and it could take anywhere from six months to several years for Deng's true successor to emerge. None of the contenders wants to spark political instability in a country experiencing massive economic change. "Stability, both politically and economically, is a main concern for them," says Shan Li, international economist for Goldman, Sachs & Co. in Hong Kong.

UPROOTED. Preserving stability will have steep economic costs, however. While Deng carried out many daring reforms that led to explosive growth, he didn't address some of China's deepest problems. The political structure is archaic and dominated by often corrupt Communist Party hacks. Large and inefficient state-run companies, relics of the Mao era, still dominate nearly half of the economy and hog an estimated 40% of the central government's resources. With no safety net to provide for displaced workers, Beijing dares not press ahead with a wave of privatizations or bankruptcies. That leaves Beijing no choice but to force its near-bankrupt banks to keep credit flowing to state factories, even though inflation hit 25% last year.

As a result, the new central leaders

will face a tough choice: either to allow high inflation or high unemployment. If inflation spirals out of control, it could spark instability among China's downtrodden, particularly among the 100 million uprooted peasants who don't have jobs. And high inflation could also touch off worries among foreign investors. Despite those concerns, few leaders want to be blamed for an economic bust, so analysts say the government apparently has opted to stay on the high-growth track. That means risky moves such as reforming state enterprises are likely to be put on hold (table).

As Beijing tries to buy the support of

the poor, fiscal restraint will suffer. As a result, the fiscal deficit is expected to be about twice the official target of \$7.8 billion. At the same time, China will be slow to make the needed compromises on market opening to get into the World Trade Organization because state enterprises are in no position to compete with foreign multinationals.

The disparity between China's wealthy provinces and their poor inland cousins also could worsen. But it's unlikely Beijing will move to regain much of the financial latitude given to the coastal provinces under Deng because that would disrupt growth. In fact, the



SHANGHAI RIDE:
COASTAL CITIES
GET RICHER AS
THE HEARTLAND
REMAINS POOR

es of decentralization are likely to erate. Some scholars, such as David Goodman at the University of Technology in Sydney, believe China is ed for an "informal federal" structure in which Beijing deals with the inces on a flexible basis but cannot ose direct edicts on them. "Power to be shared in many different s," he says. "China is no longer the e that Mao ruled over."

ne implication is that China's door ne outside world almost cer- y will remain open. Almost no in China wants to return to old isolationist economy cham- ed by Mao Zedong. In one of most important legacies, Deng aged to root out almost all -line Communists from positions of er over the past 16 years. Virtually major factions, from local party bu- erats to the military, voice support reform.

or foreign business executives, the ng months will be dicey. In a coun- where *guanxi*, or connections, count t, the uncertain succession makes it ear which companies have *guanxi* matters. One obvious victim is the er sector: Big-ticket deals cut with leaders can unravel if they're not ed by the proper authorities in Bei-

jing—but figuring out who the right people are is difficult. For months, big deals involving companies such as General Electric Co. and Wing Group have been delayed in part by the long Deng deathwatch.

The good news is that Beijing's wor- ries about keeping the lid on domestic problems will prompt China's leaders to maintain good relations with the out- side world. There are signs that Beijing is moving toward resolving a dispute

Power may begin to slip faster from Beijing to the provinces

with the Clinton Administration over the issue of intellectual-property piracy. The Administration has issued a Feb. 4 deadline for the Chinese to crack down on pirates who rip off U.S. products—and the last thing Beijing wants now is a full-fledged trade war with the U.S.

Tensions could flare up, though, over human rights violations. A jittery lead- ership is certain to continue its clamp- down on dissent. With key members of the U.S. Congress pressing for a tough- er stance on China, the two nations' re- lations could be in for a rough ride.

Even under the best of circumstanc- es, Deng's passing will subject China's leaders to their toughest period since the 1989 Tiananmen massacre. That rec- ognition has sent Asian stock markets into a selling frenzy. Since the latest rumors of Deng's death began in mid- January, Hong Kong's Hang Seng In- dex has fallen 7%. Taiwan's market plunged 4% after reports that Deng was in a coma. "Investors will step back from China over the next six months to see how the succession plays out," says William R. Ebsworth, chief investment officer at Fidelity In- vestments Management Hong Kong Ltd.

Despite the sell-off, most direct foreign investments are committed for the long haul. "The forces of capital- ism are overwhelming," says David M. Friedson, president and CEO of Miami Lakes (Fla.)-based Windmere Corp., a \$180 million manufacturer of small appli- ances. His company is adding 13% more capacity to its 1.5 million-square-foot Shenzhen factory this year.

Indeed, from the biggest multination- als to the small original equipment man- ufacturers, many executives doing busi- ness in China are used to riding out the vagaries of its topsy-turvy political system. They are prepared to invest



ECONOMIC REFORMS

A prolonged struggle could jeopardize some central government initiatives but allow local leaders more leeway

AT RISK

- ★ The central government's effort to control inflation and bank credits
- ★ Efforts to reform the national financial system
- ★ Attempts to devise a national taxation system
- ★ Approval of big-ticket foreign investments
- ★ Privatization of inefficient state enterprises
- ★ Freeing up pricing of certain staples

PROCEEDING

- ★ More ties between coastal regions and Hong Kong, Taiwan, and South Korea
- ★ Deals at provincial level for foreign companies
- ★ Growth of businesses in the nonstate sector
- ★ Opening of key sectors like telecoms
- ★ Provincial resistance to paying taxes to Bei- jing and to heeding the center's edicts
- ★ Increasing disparity between wealthy coastal provinces and poor interior

DATA BUSINESS WEEK



AN

DISASTER, YES. CRIPPLING BLOW, NO

ns point to continued growth in Japan despite the quake

y many measures, Takaaki Hashizume is a ruined man. The earthquake that hit Kobe on Jan. 17 destroyed his rented house and a restaurant he had built on the first floor. Hashizume, 46, wasn't insured against a quake and has minimal savings. But he's in the mouth? Hardly. As they ate dinner over wood scavenged from home, Hashizume and his family are asked to offer some rice gruel to a currier-reporter. "If we think about the future too much instead of eating what we have, we'll just lose spirit," Hashizume says. He reckons he'll open a new restaurant when the rubble clears.

With that kind of pluck, Japan may be able to continue and even accelerate halting economic recovery that began last year. Despite the market's dead but nervous reaction to the quake on Jan. 23, when the Nikkei stock index fell by 5.6%, many economists and company executives remain sanguine about Japan's economic prospects. There will be pain, they say, but it is unlikely to reverse upward trends in consumer spending and industrial growth. Even the bullish is Chris Calderwood, an economist at Barclays de Zoete Wedd Research Ltd. in Tokyo: "We expect a significant acceleration in growth." He's predicting 2.5% for this year (chart).

A key reason for the optimism is consumer spending. It has been rising for

several months as a stronger yen, deregulation, and bargain-hunting have brought prices down and consumers back to stores. Except for a short-term jolt to consumer confidence after the quake, spending is likely to continue—especially if worker bonuses rise this summer. Sinking real estate values and an expansion of government subsidies had bolstered demand for new homes even before the temblor. A \$55 billion income-tax cut and a plateauing of unemployment at 3% are giving an added kick to consumer sentiment. At Tokyo Mitsubishi Motor Sales, President Akira Kawakami expects to sell 5% to 8% more cars this year than in 1994. "Things are finally picking up again," he says.

PROFITS UP. There are other pockets of strength. Industrial production rose for the fourth straight quarter from October through December, according to the Bank of Japan. Corporate profits will likely surge up to 60% this year, as the benefits of recent restructuring are realized. "During the past two years, we have completely reshaped our cost structure," says Tatsuro Toyoda, presi-

SUSTENANCE: Returning to a shelter with emergency food supplies

dent of Toyota Motor Corp. The company says that in its fiscal year ended last July, it cut costs by \$1.5 billion.

With \$20 billion in the bank, Toyota isn't the only Japanese company flush with cash. And these full pockets may produce a modest resurgence in capital spending. Such expenditures declined for 11 straight quarters until a 0.5% rise in the third quarter of last year. Barclays de Zoete Wedd predicts a 1.7% gain this year and 3.2% next year. NEC Corp., for example, has budgeted more than \$1 billion to refurbish its Kumamoto semiconductor plant.

But for now, companies and consumers will have to cope with the short-term economic pain of the quake's aftermath. Lost production and shipments from the quake area, which accounts for about 12% of gross national product, could pull down first-quarter growth to 1.3%, says Peter Morgan, chief economist at Merrill Lynch Japan Inc.

SPENDING LULL. This could be exacerbated by a propensity of frightened Japanese to spend less. The trend is already showing up in sales in Tokyo department stores, which have fallen 7% to 11% since the quake. But most economists expect just a brief setback followed by extra spending for replacement of the possibly \$200 billion worth of damages, adding between 0.3% and 1.5% to 1995 GNP growth and as much as five percentage points to GDP growth over the next five years.

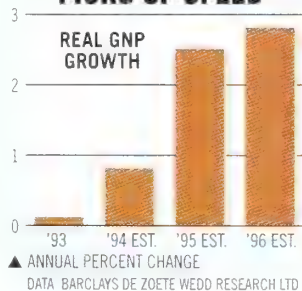
Some experts fret that supply disruptions may fuel inflation and that demand for capital may hike interest rates. But most think that the Bank of Japan will be wary of tightening the money supply, which has been growing. What's more, Japan is in relatively good fiscal shape. It has the confidence of the world's major economies and a low debt level compared to GNP. Says Tod Wood, an economist at Baring Securities (Japan) Ltd: "They will be able to finance this."

Consumer confidence might yet be shaken.

"The issue is when the rebuilding stops and people realize the country is relatively poorer," says Masaru Kakutani, a managing director at Moody's Japan. But so would be any country suffering a disaster of this size. Japan is lucky its economy can more or less afford it.

By Robert Neff in Tokyo, with Larry Holyoke in Kobe

JAPAN'S ECONOMY PICKS UP SPEED



DEALS

LONDON BANKS ARE TEAMING UP, TEAMING UP

For investment bankers, the lucre lies in a global reach



It has been nearly a decade since London's Big Bang, when the government at one fell swoop lifted regulations that had kept the investment banking industry a patchwork of specialty brokers, market-makers, and merchant bankers. A handful of mergers later, there's still an informal division of labor between banks that underwrite equity and debt issues and those that sell them. And the securities business remains fragmented, with three dozen major investment banks battling each other for business.

But the crowded field may soon thin out. Investment bankers predict that the City of London could soon resound with an echo of the Big Bang. "There are going to be mergers and takeovers, and I think some may actually happen soon," says Peter Letley, deputy chairman of HSBC Investment Banking Ltd. "A number of players in the London market are not sufficiently global."

POND JUMPERS. A fear of being insufficiently global is precisely what propelled Britain's premier investment bank, S.G. Warburg Group, toward Morgan Stanley & Co. in mid-December. And on Jan. 25, London's Govett & Co. announced plans to merge with Chicago-based Duff & Phelps Corp. in a \$250 million deal that creates a global asset management and equity research house with \$50 billion under management.

While the marriage of convenience between Warburg and Morgan Stanley was reported a week later, the logic behind

it remains: To be successful, investment banks need to offer corporations a wide range of products in numerous markets outside their home base. Today's most lucrative action is in cross-border deals, and London banks are losing juicy business to players with a longer international reach. U.S. banks are even horn-in on strictly domestic deals. In Glaxo Group's surprise \$14 billion bid for fellow British drugmaker Wellcome PLC on Jan. 23, Wellcome is being advised not only by Barings PLC, a second-tier London merchant bank, but by Morgan Stanley, too.

The biggest squeeze is coming from the U.S. heavyweights, especially Goldman Sachs, Merrill Lynch, and Morgan Stanley. Merrill Lynch is now widely recognized as the powerhouse in debt securities of all kinds. Goldman Sachs is the worldwide leader in mergers. Morgan Stanley ranks No. 3 in worldwide equity issues. Meanwhile, the big Continental banks are also beefing up their London operations.

The stakes are getting higher all the time. With corporate profits recovering

MUSCLE BOUND To compete, merchant banks are turning to foreign powerhouses

in Europe and the U.S., record levels of equity deals, debt issues, and mergers are expected for 1995. However, the problem for London's banks is that more deals are congregating in fewer hands. Of \$76 billion in M&A deals in Europe in 1994, for example, five banks acted as advisers for 65% of them, when ranked by dollar value. Of the five banks, three were American.

TRY, TRY AGAIN? No wonder the consolidation rumors are flying. Warburg officials deny that they are looking for another suitor, but with the company's share price rising 15%, to \$12, in the past two weeks, the market clearly thinks otherwise. Independent London brokers Smith New Court and Panmure Gordon, owned by NationsBank, also are "obvious takeover targets," says HSBC's Letley. The two banks would not comment. Other prominent British houses considered takeover bait include Robert Fleming, Hambros, and Lazard Brothers—but any overtures would have to be friendly, since each is family owned or controlled.

At the same time, Europe's big banks are plotting to acquire the critical mass and trading expertise to compete with the U.S. powerhouses. Deutsche Bank just moved much of its investment banking operation to London, where it previously had scooped up merchant banker Morgan Grenfell Group. Banking sources say that Deutsche is considering making an offer for Cazenove & Co., a highly secretive broker with a blue-chip client list. Deutsche and Cazenove both declined to comment. Deutsche's German archrival, Dresdner Bank, and Union Bank of Switzerland have both been named as possible suitors for Warburg, although Dresdner officials decline comment and UBS denies any interest.

Some London merchant banks are trying to hang on to their independence by aiming for a niche. Privately owned Barings has a powerful franchise in emerging markets and is targeting smaller institutional investors and private clients. Schroders PLC has built a successful investment arm, with \$94 billion in funds under management. Also, instead of chasing big deals, it's going after project finance work in emerging markets.

Nevertheless, in August, Schroders quietly bought the remaining half of its U.S. partner and equity distribution arm, Wertheim Schroder & Co., in a \$94 million deal, and plans to use Wertheim to expand into Latin American equities. Clearly, even for London's successes, the siren they hear is far offshore.

By Paula Dwyer in London

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EDITED BY STANLEY REED

IF THE CENTER CANNOT HOLD, WILL GERMANY'S LEFT RISE?

For decades, Germany's Free Democratic party (FDP) has played kingmaker in Bonn. As a centrist third party with a solid block of Bundestag seats, it has held the balance of power between the huge, conservative Christian Democratic Union (CDU) and the socialist Social Democratic Party (SPD). In 1982, for example, it brought the CDU's Helmut Kohl into office by ditching SPD Chancellor Helmut Schmidt.

Now, as Germany prepares to move the government to Berlin by 2000, the FDP risks being marginalized just as the old capital, Bonn, will be. The FDP's staple formula of free-market economics and an eastward-looking foreign policy no longer plays with the voters. It's considered the party of smug, well-heeled and aging Germans.

The FDP did manage to put Kohl over the top in the general elections last October, but it saw its share of the vote nearly halved, from 11% to 6.9%. That was perilously close to the 5% necessary to qualify for seats in the Bundestag.

GOOD SHOT. Many younger voters and east Germans, who are not attracted to the major parties, are turning instead to the environmentalist Greens and the reformed communist organization, the Party of Democratic Socialism (PDS). Although some of their policies, such as wanting to leave NATO, are still impractical, the Greens have a good shot at replacing the FDP as the major third force.

The weakening of the FDP could have profound consequences for Germany. Just as the country is struggling to cut social spending and make its industry more efficient, a key voice for market reforms, privatization, and deregulation will be muted. It will become much tougher to cut spending or reduce taxes on business. Indeed, with the Greens and PDS

having substantial blocs of seats, it will become easier to form left-wing coalitions, and German politics could be subject to more volatile swings without the FDP's stabilizing influence.

The FDP's decline could even force Kohl to cut short his four-year term. Political analysts worry that in an effort to revive their appeal, FDP Bundestag members may abandon the Chancellor in midterm, as they did Schmidt in 1982. With Kohl holding a slim 10-vote majority, "it only takes six desperadoes to topple the coalition," warns Bonn-based political consultant Heinz Schulte.



NEW FACES: A shift in the Bundestag

Politicos are closely watching a series of coming state elections. If the FDP fails to reach 5% in one or more, panic could set in. The first vote will take place on Feb. 19 in Hessen, which includes Frankfurt. "I am trying to convince my party not to get nervous," says former FDP Chairman and elder statesman Otto Lamsdorff. But he concedes: "The reaction to the results could be very damaging."

POOR SHOWING. Some analysts say that unless the FDP chalks up some convincing wins soon, it is doomed to be swept out of the next Bundestag in 1998. Chances of a turnaround

don't seem good. Since 1992, the party has not won a single seat in any state legislature. It has now been booted from nine of Germany's 16 state parliaments.

The FDP's decline at the state level benefits not only the Greens but the socialists, currently led by Rudolf Scharping. Although they haven't done well in national elections in recent years, the socialists now have the biggest blocs in the majority of the state governments, which they run in coalitions with the Greens, the PDS, and even the CDU. That could augur a sooner-than-expected return of the left to national power.

By John Templeman in Bonn

GLOBAL WRAPUP

WALLING OFF THE WEST BANK?

► The death of 19 Israelis in a Jan. 22 bombing attack in central Israel has prompted the government to take its most serious look yet at the feasibility of total separation from the territories of Gaza and the West Bank. Prime Minister Yitzhak Rabin is proposing the establishment of a Cabinet-level committee to study the economic and security considerations of such a step. The most difficult problem confronting the Israelis would be what to do about their 150,000 set-

tlers who now live in the West Bank.

Rabin has already ordered the territories sealed off from Israel—as he has done many times in recent years following similar incidents. Finance Ministry sources say that a permanent cutoff from the territories would not be that disruptive to the Israeli economy, because with a gross domestic product of \$75 billion, it is more than 30 times the size of the Palestinian economy. The number of Palestinians who travel to Israel to work each day has already been cut to about 60,000 from a peak of some 130,000

several years ago. Israel has brought in about 50,000 workers from Asia and Eastern Europe to take jobs in agriculture and construction.

Long-term separation, however, would be devastating to the Palestinian economy. Despite their animosity toward Israel, Palestinians get much of their income from work in the Jewish state. If they are kept out, tension in the occupied territories is likely to increase, making Yassir Arafat's already shaky grasp on power even more tenuous.

By Neal Sandler in Jerusalem

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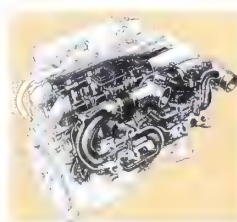
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*Car and Driver magazine, mid-1994 publication
September 1993

FISCAL POLICY

THE GOP'S BRUTAL BOTTOM LINE

A balanced budget without deep, agonizing cuts? No way

"Once members of Congress know exactly, chapter and verse, the pain that the government must live with in order to get a balanced budget, their knees will buckle."

—House Majority Leader Richard K. Armey (R-Tex.)

The GOP-controlled Congress is on its way to approving a balanced-budget amendment to the Constitution. But Armey is right about the agony. States may see federal aid slashed by at least one-third. Local taxes would rise. Medicare patients would have fewer health-care choices and pay more for them. Welfare for poor mothers and children would be slashed. Subsidies to farmers and small businesses would be trimmed. And costs of everything from college loans to airplane tickets would surely rise.

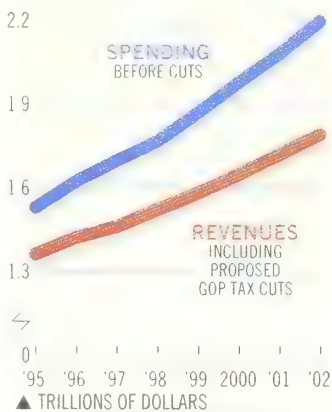
With programs such as these on the chopping block, it's no wonder Republicans aren't saying how they would fulfill their Contract With America. They have pledged to balance the books by 2002 while allowing for more defense spending and cutting taxes by \$370 billion—without trimming Social Security or raising other taxes. To make the rhetoric real, BUSINESS WEEK put together a representative package of cuts. These aren't necessarily the exact changes the GOP would make, but they provide a sense of how the Contract would change government.

GOP deficit-cutters can't escape their own bottom line: They'd have to slash planned spending through 2002 by an

eye-popping \$1.5 trillion, or more than 20% for programs other than Social Security and defense. House Speaker Newt Gingrich (R-Ga.) claims that savings can be achieved by reducing the rate of government growth. But deep cuts are unavoidable, even for the middle class, which has been largely sheltered from past deficit-trimming. "It would radically change the character of government,"

SHARPEN THE AX, NEWT

After cutting taxes, balancing the budget by 2002 gets even tougher



DATA: CONGRESSIONAL BUDGET OFFICE
TREASURY DEPT., BUSINESS WEEK

says Iris J. Lave, associate director of the Center on Budget & Policy Priorities.

On the plus side, businesses may be liberated from government red tape. Companies, middle-class families, and investors could pocket juicy tax cuts. The biggest payoff could come from sharply lower interest rates. DRI/McGraw-Hill estimates that a balanced budget in 2002 would drop rates on 10-year government bonds by two percentage points, boost business and housing investment by 6%, and hike annual economic growth 0.25%.

In that light, a big drop in spending may be desirable. Says Conference Board Chief Economist Gail D. Fosler: "This kind of restraint helps in a period of sustained growth."

But how would lawmakers get to balance? The GOP's favorite targets are welfare, foreign aid, and programs of the "cultural elites"—the National Endowments for the Arts & the Humanities and the Corporation for Public Broadcasting. Shuttering the endowments and CPB would save a paltry \$4 billion over seven years—0.2% of what's needed. Squeezing welfare by one-third would pick up \$40 billion by 2002. Chopping foreign aid in half would produce an additional \$70 billion. But when you need \$1.5 trillion, this is chicken feed.

For bigger bucks, the GOP will have to cut up to \$560 billion in projected domestic discretionary spending over the next seven years. A few sacred cows might be spared the ax—including pris-



ons, courts, and most veterans benefits—but nearly everything else would get chopped. Amtrak would be privatized, so would the air-traffic-control system—saving about \$50 billion through 2002. Airport-construction grants and mass-transit operating subsidies would be dumped, picking up \$16 billion. The federal power-marketing agencies, which provide low-cost electricity to the South and West, would be sold. Programs such as the Appalachian Regional Commission and Community Development Block

Gingrich claims the gap can be closed by slowing the growth of spending, but his numbers don't add up

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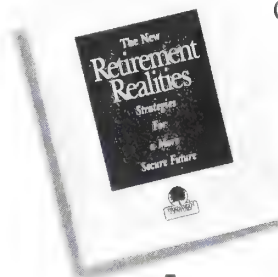
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...and on-again: Visitor fees at national parks might triple, raising \$1 billion. And entire Cabinet departments might vanish, though the savings would still be relatively small. Shuttering the Education Dept.—including many student-loan programs—would save about \$210 billion through 2002. Yet after all that, deficit-cutters would only be about 16% toward their goal.

The real money—\$900 billion through 2002—would have to come from politically sensitive “entitlements,” such as subsidies for farmers, health care for the aged and poor, and retirement benefits for federal employees. By protecting Social Security—22% of the budget by 2002—the GOP must target the big health programs. In a sense, the sick and infirm would pay to protect healthy pensioners. “You can’t seriously tackle the deficit without making significant savings in Medicare and Medicaid,” argues the Heritage Foundation’s Robert E. Moffit.

DAUNTING TASK. In the past, budgeteers could squeeze payments to doctors and hospitals and tinker with patient premiums. But it will take far more than that this time. One possibility: pushing new retirees into managed-care plans, such as health-maintenance and preferred-provider organizations. That could cut Medicare spending by \$250 billion over seven years. Doing the same for Medicaid, which serves many elderly in long-term care and poor women and children, could save an additional \$120 billion.

The task is so daunting that for the GOP to keep its promise—balancing the budget while cutting taxes, boosting military spending, and leaving Social Security untouched—it could freeze all other spending at 1995 levels for seven years yet still might not meet its goal. And, assuming 3% inflation, such a freeze would slash federal purchasing power by 23%.

That leaves the GOP with few choices. It can freeze defense spending or drop some of its tax-cut ideas. Republicans also want government inflation measures recalculated, which could save \$200 billion over seven years. But that means lower cost-of-living hikes for Social Security recipients and reduced inflation adjustments for taxpayers’ standard deductions and personal exemptions. And that sounds a lot like a backhanded Social Security cut and a tax hike—both Contract no-no’s.

There is, of course, another alternative—passing a Constitutional amendment but not actually balancing the budget. And as the choices get tougher, the GOP may try to find a way to do just that. One House Republican has just the solution: “I’m going to vote for the amendment. And then I’m going to pray and hope that the states don’t ratify it.”

—MONTY MAZUR
—WASHINGTON

The Corporation

STRATEGIES

BOMBARDIER'S BLITZ

Zooming to become a world player in railcars and jets

In February, Chinese railroad officials will descend on La Pocatière, Que., a town of under 10,000 nestled beside the St. Lawrence River. From its sprawling plant here, Bombardier Inc. has taken a commanding position in the North American market for mass-transit equipment. At La Pocatière, the company has built subway cars for New York, double-deck Superliner cars for Amtrak, and monorail cars for Walt Disney World Co.

Now, the Chinese want Bombardier to share this technology. Under a tentative joint venture announced last November, Bombardier will help manage China’s largest passenger-rail factory. The agreement would give Bombardier a toehold in the world’s largest market for mass-transit gear.

If the deal goes through, it will be just one more example of Montreal-based Bombardier’s emergence as a global powerhouse. In Malaysia, Bombardier recently won a contract to build a 20-mile light-rail system in Kuala Lumpur. In the U.S., Bombardier’s 50-seat Regional Jet is helping revolutionize commuter airlines by letting carriers provide economic jet service to small cities. And in Europe, where it built the high-tech railcars now hauling cars and buses through the Chunnel, “I would put Bombardier in the same league as Siemens, GEC-Alsthom, or ABB,” says Eurotunnel Chairman Sir Alastair Morton.

SNOW JOB. All this has helped Bombardier more than triple sales since 1989, to \$3.4 billion in fiscal 1994, while profits were up 157%, to a record \$125 million. Bombardier’s stock, at 17, has grown at a compound annual rate of 33%. Fiscal 1995, which ends on Jan.

31, looks even better. Through the first three quarters, Bombardier’s income soared 40% on a 12% sales gain.

That’s a far cry from its early days. When CEO Laurent Beaudoin took the reins of Bombardier in 1966, he was just 27, and the company—with only one major product, the Ski-Doo snow-

A DIVERSE PRODUCT MIX...

1994 EARNINGS: \$125 MILLION	1994 SALES: \$3.4 BILLION
INDUSTRY/KEY PRODUCTS	PERCENT OF FISCAL 1994 SALES
 AEROSPACE Business and regional/commuter aircraft, including: Learjet, Challenger business jets	54%
 RAIL TRANSPORTATION EQUIPMENT Train cars for the Chunnel, subway cars for New York, Boston and Mexico City, Superliner coaches for Amtrak, mass transit systems for Ankara and Kuala Lumpur	27%
 MOTORIZED CONSUMER PRODUCTS Ski-Doo snowmobiles, Sea-Doo personal watercraft	17%
 BOMBARDIER CAPITAL GROUP Financial services	2%

...AND GLOBAL REACH

BOMBARDIER'S 1994 SALES BY ECONOMIC REGION

U.S., MEXICO 43%
CANADA 10%
ASIA, REST OF WORLD 6%
EUROPE 41%

DATA: BOMBARDIER INC.

mobile—had annual sales of some \$15 million. “I had to learn on the job,” the 56-year-old Beaudoin recalls. Along the way, Beaudoin has made Bombardier a global force in three industries: rail and mass-transit equipment; aerospace, including business and regional jets; and consumer products such as snowmobiles and watercraft (table).

Beaudoin accomplished the makeover through a risky strategy of buying a string of nearly bankrupt companies

he vows to double Bombardier's sales over the coming five years without making major acquisitions. It's an ambitious goal, since many of Bombardier's markets are mature and the competition cutthroat. But Beaudoin is at his best when facing a challenge. His first one came less than a year after he joined Bombardier as comptroller in 1986. Only nine months after he arrived, his father-in-law, Joseph-Armand Bombardier—who had invented the snowmobile—died of cancer. Beaudoin was promoted to general manager, and in 1987 he was named president, just as the snowmobile craze swept North America.

GOING RIGHT. When the 1973 energy crisis wiped out all but 4 of the 100 automobile manufacturers, Beaudoin strategically diversified. The key deal was a contract to make 423 subway cars for Montreal. Today, Bombardier has a third of the North American market for mass-transit equipment and five plants in Europe. "Their manufacturing knowhow is

about aerospace," Beaudoin declares.

Maybe not. But Beaudoin "has an incredible sense of smell," says board member and Harvard business school professor Hugo Uytterhoeven. At Canadair, Beaudoin scented the chance to move into two niches where his company could excel: business jets and regional aircraft. To round out Canadair's product line, he snapped up three other sick plane makers: Boeing's hemorrhaging de Havilland unit, business-jet pioneer Learjet, and Short Brothers, Northern Ireland's largest employer. Since then, his management team has turned all four around by melding them into a competitive whole.

In early 1990, for example, Wichita's Learjet was in a seemingly uncontrollable nosedive. But Beaudoin didn't sack Learjet President Brian Barents, who had a credible turnaround plan. What the company needed was money. That fall, Lear announced it would spend \$100 million on a new intercontinental

Fred George, a pilot and a senior editor at *Business & Commercial Aviation*.

Over the coming five years, "most of our growth will come from such new products," says Beaudoin. He also has big expectations for the Global Express, a new long-range jet that cost \$800 million to develop, (page 66) and the \$200 million Regional Jet (RJ). Although the 50-seat RJ got off to a slow start when it hit the market in 1992, it is now taking off. Before the RJ, "there was no jet in the 50-seat range with decent economics," says SkyWest Inc. Chief Executive Jerry C. Atkin. With the RJ, SkyWest can break even flying just 25 people from Salt Lake City to Rapid City, S.D., vs. the 90 to 100 people it took with bigger jets. In December, Lufthansa's regional carrier, CityLine, ordered eight RJs, pushing Bombardier's backlog to 42.

CHINA CHOO-CHOO. The other engine of Bombardier's growth is a stronger push into new geographic markets. Last year, 53% of Bombardier's sales came from North America and 41% from Europe. But in November, Bombardier cinched its largest Asian contract yet: a \$400 million role in Kuala Lumpur's \$2 billion light-rail system.

The joint venture Bombardier is negotiating with the China National Railway Locomotive & Rolling Stock Industry (LORIC) has far bigger potential. Under the deal, Bombardier would bring LORIC's plant near Qingdao up to world-class standards. Railcars built there would then be sold throughout Asia. If the deal succeeds, "Bombardier would have a substantial lead over its competitors," says Normand Roy, an analyst at Montreal's Lévesque Beaubien Geoffrion Inc.

Beaudoin has already learned a few hard lessons about operating in emerging markets. After the company paid \$22 million to buy Concarril from the Mexican government in 1992, it assumed it had a lock on Mexico. But just six months later, it was beaten by a Spanish competitor for a contract to supply cars to the Mexico City subway.

Only then did Bombardier hire Miguel Yoldi, a Mexican consultant, to run Concarril. Yoldi's advice: "It's very difficult to do business in Mexico if you don't develop a relationship and build trust." Bombardier quickly dropped a legal challenge to the Spanish deal and began cultivating Mexican officials. Although the peso crisis will slow its projects, Beaudoin still considers Mexico one of Bombardier's better prospects.

Still, globalization hasn't come without problems. Although Bombardier beat out stiff competition to win a \$575 million contract to build shuttle-train cars for the Eurotunnel consortium, costs



ing the best in the world," concedes Aram Martinsen, president of archrival Siemens Transportation Systems Inc. It wasn't until Beaudoin sought to bring Bombardier into aerospace in 1986 that his savvy at dealmaking became apparent. His first target: Canadair. The government-owned aircraft maker was drowning in debt and had only one viable product: the Challenger, a regional business jet. The company looked feeble, and "we knew nothing

about aerospace," Beaudoin declares. Maybe not. But Beaudoin "has an incredible sense of smell," says board member and Harvard business school professor Hugo Uytterhoeven. At Canadair, Beaudoin scented the chance to move into two niches where his company could excel: business jets and regional aircraft. To round out Canadair's product line, he snapped up three other sick plane makers: Boeing's hemorrhaging de Havilland unit, business-jet pioneer Learjet, and Short Brothers, Northern Ireland's largest employer. Since then, his management team has turned all four around by melding them into a competitive whole.

Here's where the acquisitions paid off handsomely: The Lear 45 would have cost an extra \$40 million if Lear hadn't been able to farm out the fuselage to Short and turn over the wing to de Havilland. That helped Lear price the plane at just \$6 million, which will make it "their breakthrough product," says



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soared as specifications changed repeatedly. In mid-1993, Bombardier filed a claim for an additional \$600 million. After arduous negotiations, Beaudoin settled for just \$113 million in cash, plus 25 million shares in the Eurotunnel project, then worth some \$150 million. If the shares, which have since fallen to around \$125 million, recover, Beaudoin says Bombardier will still break even on the project.

The Chunnel debacle has caused Bombardier to lose \$70 million in its transportation-equipment unit in the past two fiscal years. But thanks to diversification and booming sales of products such as Sea-Doo watercraft, Bombardier's overall net income still rose.

It's Beaudoin who personally steers the company through such turbulent waters. Few executives can keep up with his relentless pace. "He's a workaholic," says Bank of Montreal's Barrett. "He just loves what he does, and he does it 150% of the time." Barrett should know. During a weekend at Beaudoin's hunting lodge on an island in the St. Lawrence, Beaudoin "successfully harassed me on why it might be a better idea to have a plane with a Canadian flag on the tail," Barrett recalls. The pressure paid off when Barrett traded in the bank's French-built Falcon 50 for a Challenger.

Beaudoin, who relaxes by playing tennis, riding horses, and zooming through

the Quebec woods on a Ski-Doo, is showing no signs of retiring very soon. But when he does, the succession decision will belong to him and other members of the Bombardier family, who control over 60% of the corporation. Does that mean Beaudoin's son Pierre, who at 32 is managing the division that makes Ski-Dos and Sea-Dos, will succeed his father? His father insists that is far from sure. But whoever it is, he'll find himself at the throttle of one of North America's most thoroughly international companies.

By William C. Symonds in Montreal with Farah Nayeri in Paris, Geri Smith in Mexico City, and Ted Plafker in Beijing

A DOGFIGHT OVER 950 CUSTOMERS

For three decades, Gulfstream Aerospace Corp. has dominated the market for that *ne plus ultra* of corporate high life: the large business jet. Gulfstream's customers for its current jet—the \$27 million G-IV—include General Electric Co.'s John F. Welch, Walt Disney Co.'s Michael D. Eisner, and such stars as Bill Cosby. Appropriately, Gulfstream itself is owned by Wall Street's elite Forstmann Little & Co., which bought it from Chrysler Corp. for \$825 million in 1990.

But suddenly, Gulfstream is flying into a dogfight. Bombardier Inc. is spending \$800 million to develop a plane aimed at surpassing Gulfstream as the ultimate corporate jet. Bombardier's Global Express jet will be able to whisk a CEO nonstop from New York to Tokyo or Beijing. At a cost of up to \$33.5 million—including several millions for plush cabins that include conference tables and full-size beds—it will offer comforts that first-class passengers on commercial carriers can barely imagine. "We will become the major player in this market," predicts Bryan Moss, president of Bombardier's Business Aircraft Div.

EARLY BIRD. In a closely guarded "war room" at Savannah (Ga.) headquarters, Gulfstream executives are tracking every detail of Bombardier's flight plan as part of a drive to get their own ultralong-range jet, the G-

V, into the skies first. Like the Global Express, a fully equipped G-V will cost about \$35 million and fly 6,500 nautical miles nonstop. But while the Global Express won't be delivered until 1998, the first G-Vs will be

COOL \$33 MILLION: *The Global Express from Bombardier's Canadair will not be ready for market until 1998*



available in 1996.

"We'll have 40 G-Vs operational before their first one taxis into a hangar," says Rainer Revitz, Gulfstream's marketing head.

Some observers wonder if either company will make money. "It will be a limited market," warns Roger N. McMullin, CEO of Aviation Methods Inc., provider of private-jet services to 25 corporations. Even Bombardier admits that no more than 950 multinationals, billionaires, and heads of state are apt to buy one of the two jets. Skepticism also reigns at rival Dassault Aviation, which dropped plans to enter the fray. "A lot of CEOs wonder if it is justifiable to spend this kind of mon-

ey to fly nonstop [to Asia] five or six times a year," says a Dassault executive.

To reduce its own risk, Bombardier has assembled a team of partners. They include BMW, Rolls-Royce, Mitsubishi Heavy Industries, and Honeywell. Bombardier will shoulder just 40% of development costs, so Moss says it needs to sell only 100 planes to break even.

Since business jets are Gulfstream's only product, this is a battle it can't afford to lose. Gulfstream believes it can develop the G-V for just \$300 million, largely because it's building on the proven G-IV and incorporating suggestions from some loyal customers. Certain industry observers predict that the actual bill will hit \$400 million. Either way, it's a

burden that Gulfstream—which canceled a 1992 stock offering for \$100 million due to lack of investor interest—cannot easily bear.

So far, the contest is almost a dead heat. Gulfstream claims it has \$2 billion in orders for the G-V. About 50 buyers, including Seagram Co., have put down a \$2 million deposit. That's slightly ahead of the "over 40" orders that Bombardier says it has received. "I don't see a clear winner emerging," says John Zimmerman, president of Aviation Data Service Inc. in Wichita. Still, even a tie would be a big victory for upstart Bombardier.

By William C. Symonds in Montreal and David Greising in Savannah, Ga.

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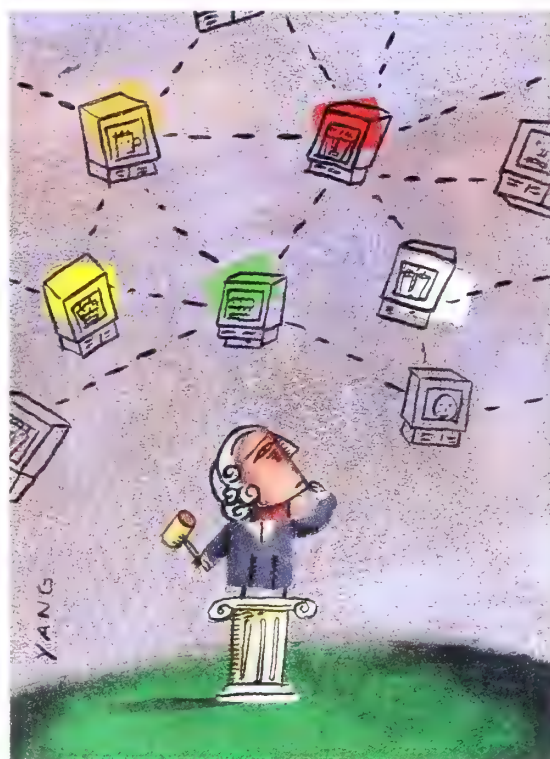
FLAMED WITH A LAWSUIT

Will courts set limits on the freedom of cyberspeech?

Stratton Oakmont Inc. is no stranger to trouble. The Lake Success (N.Y.) investment bank last year settled charges with the government that it had engaged in an illegal penny-stock scheme. But its executives found themselves in unfamiliar territory this fall when a user of Prodigy Services Co., the popular online computer service, accused the firm of fraud stemming from one of its initial public offerings. The user said Stratton Oakmont disclosed that a client had lost its biggest customer only after it launched the offering. "This is fraud, fraud, fraud, and criminal!" the user wrote on Oct. 23 on Money Talk, an electronic bulletin board operated by Prodigy.

Stratton fired back—not on the bulletin board, but in court. It filed a \$200 million libel suit on Nov. 7 against Prodigy, based in White Plains, N.Y., and John Doe, the anonymous flamer. Stratton argues that Prodigy, which removed the derogatory remarks from its network on Nov. 11, is responsible for all communication on its service. "If Prodigy is in the publishing business, then it opens itself up to libel charges," says Stratton lawyer Jacob H. Zamansky.

Stratton's case has brought to a head a long-anticipated clash between traditional law and freewheeling computer communications. Courts, businesses, and



cybernauts are all now grappling with how to control the burgeoning online technology revolution, which lets users broadcast messages worldwide, without choking off free speech. The basic problem: Existing laws are outdated for today's direct, real-time communications.

Aside from libel issues, copyright and pornography laws are also bumping up

against the tenets of the virtual world (table). And experts predict that other thorny legal questions, such as intellectual-property and contract disputes, online sexual and racial harassment, and the use of electronic communication to peddle fraudulent sales schemes, will emerge as more consumers get hooked in to the online world. In 1994, 5.2 million people logged on to commercial networks, up from 1.72 million in 1990.

The stakes in these legal contests, which threaten to dilute the in-your-face culture of cyberspace, are extraordinarily

high. Up until now, the broad appeal of the online world has been that it enables all its users to express—and defend—themselves without inhibition. But cyberexperts say court rulings that curtail such free speech could substantially cripple the budding online industry, a \$1 billion business made up primarily of eight commercial operators. "The law is designed to protect people who have no ability to reply," says Ellen M. Kirsh, general counsel of America Online Inc., based in Vienna, Va. "But the rules do change in cyberspace," where everyone can respond. (BUSINESS WEEK is an America Online partner.)

CHAINED MELODY. Stifling the growth of online services isn't the only potential danger. Unless a solution for governing electronic communication is found soon, many computer experts fear an unparalleled litigation explosion. "If every person takes offense at everything on the Net, there wouldn't be enough resources in the infinite galaxy to cover the lawsuits," says

David Banisar, an attorney at the Electronic Privacy Information Center in Washington. That is why the cyber industry will meet in February to discuss self-regulation and possible legislation. It hopes to find an ally in House Speaker Newt Gingrich (R-Ga.), a technoid who touts electronic communications as the route to greater democracy

Legal Clashes In Cyberspace

LIBEL

Should online services be held liable for inflammatory statements posted by their subscribers? Courts will soon decide whether online companies are merely vendors, like bookstores, or have editorial control, like newspapers.

COPYRIGHT

Can online services be held liable for copyright infringement even if they don't know of their subscribers' misconduct? Cyberfirms say they should only be blamed when they know about infringement and fail to take action.

JURISDICTION

Which laws govern illegal acts on electronic bulletin boards? With pornography, for example, do laws where the computer user is located apply, or should a bulletin board group be allowed to establish its own standards, superseding local law?

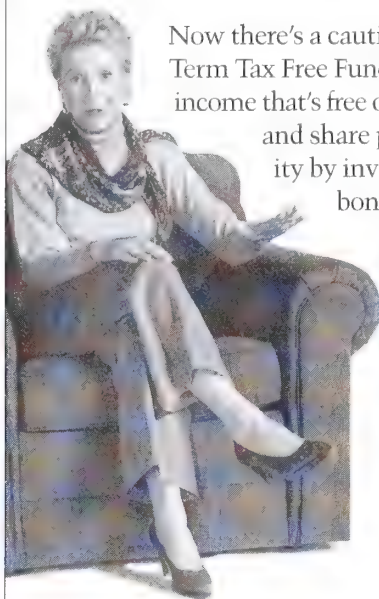
online service companies are looking Washington and internally in the es of avoiding standards imposed by ts that would be virtually impos- e to meet. CompuServe Inc., in Co- us, Ohio, for one, has found it hard police the activities of thousands of scribers using its network daily. And argues that users don't want to feel they're under constant scrutiny. the Information Superhighway, e of us wants a patrolman observing a of our actions," says Kent D. key, CompuServe's general counsel. tuckey is currently fending off a filed in 1993 against CompuServe New York-based music publisher nk Music Corp. The company accus- CompuServe of infringing the 1955 ight of *Unchained Melody* and at t 550 other compositions the music isher owns. Frank Music claims that puServe is liable for the infringe- t even if it didn't know that its sub- bers were posting and downloading ected works owned by Frank Music. puServe says it shouldn't be made ay for such acts on its network un- it knew about them and deliber- y ignored them.

online services are also struggling a jurisdictional questions; that is, se laws should govern online activity originates in one locality but has an ct on users in other regions. For mple, Robert and Carleen Thomas, ran an adult bulletin board based in itas, Calif., are now appealing a e conviction on obscenity charges by S. court in Memphis. Because ob- ity is traditionally determined by l community standards, pornogra- downloaded in Tennessee may be e offensive to locals than the same erial viewed in California.

THE HOOK. To clear up the jurisdic- al confusion caused by communica- s traversing the globe, online compa- prefer a community standard ermined by bulletin board users nselves, rather than a myriad of -world local rules. "Geography ld have nothing to do with it," says h. "If you go into the Gay & Les- Forum, you should adopt a differ- standard from Christianity Online." or the moment, the Prodigy libel as taken center stage because it is ect test of how far First Amend- t protections will go in cyberspace. its part, Prodigy says existing libel s governing media such as newspa- s, which are responsible for their ent, don't apply to it because it can't —or even read—the 75,000 notes smitted on its network daily. Bes- s, "there's no way in most cases ou could even tell whether some- g was [strictly] libel," says Prodi-

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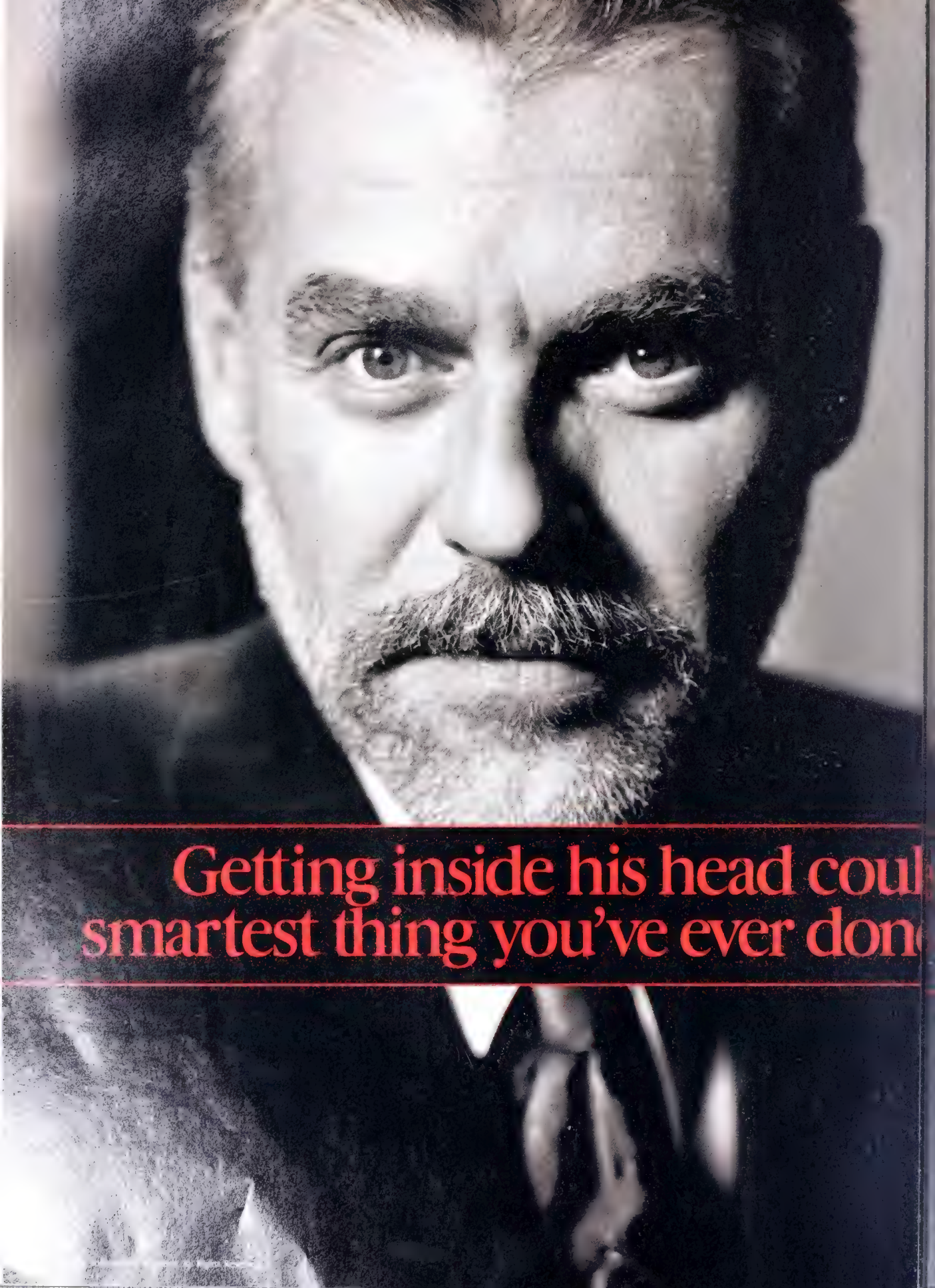
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 ... and other online defenders ...
 ... hopefully to a 1991 ruling that ...
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 ... newspaper, which exerts editorial con- ...
 ... but instead resembled a bookstore, ...
 ... distributes materials published ...
 ... others but isn't responsible for their ...
 ... ent. "We're like hotel meeting ...
 ... s," says David R. Johnson, chair- ...
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 ... ect. "We're responsible for good ...
 ... ce but not for what's said in the ...
 ...
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 ... -service advocates say victims of ...
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 ... most satisfying revenge—to make ...
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 ... e to call up your lawyer, you should

Instead of picking up
 the phone to call your
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out your keyboard and fire away," ...
 ... Washington journalist Brock N. ...
 ... ks, who settled a libel suit in Au- ...
 ... for a story he published on the ...
 ... net about an allegedly dubious ...
 ... eting scheme by Suarez Corpora- ...
 ... Industries, in Canton, Ohio. When ...
 ... Kirsh received a complaint last ...
 ... from a dog-food maker about elec- ...
 ... c postings disparaging its product, ...
 ... gave the company 10 hours of free ...
 ... e time to make rebuttals.
 ... at Stratton claims that its case is ...
 ... rent because Prodigy exercises ed- ...
 ... it control. Until 1992, Prodigy, which ...
 ... ets itself as a family-oriented ser- ...
 ... read all its subscribers' notes be- ...
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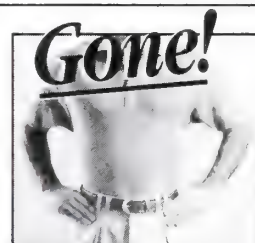
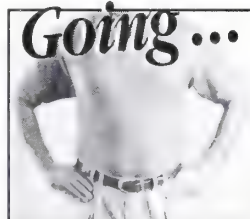
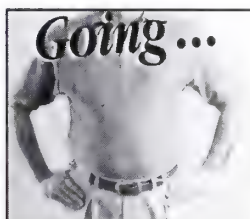


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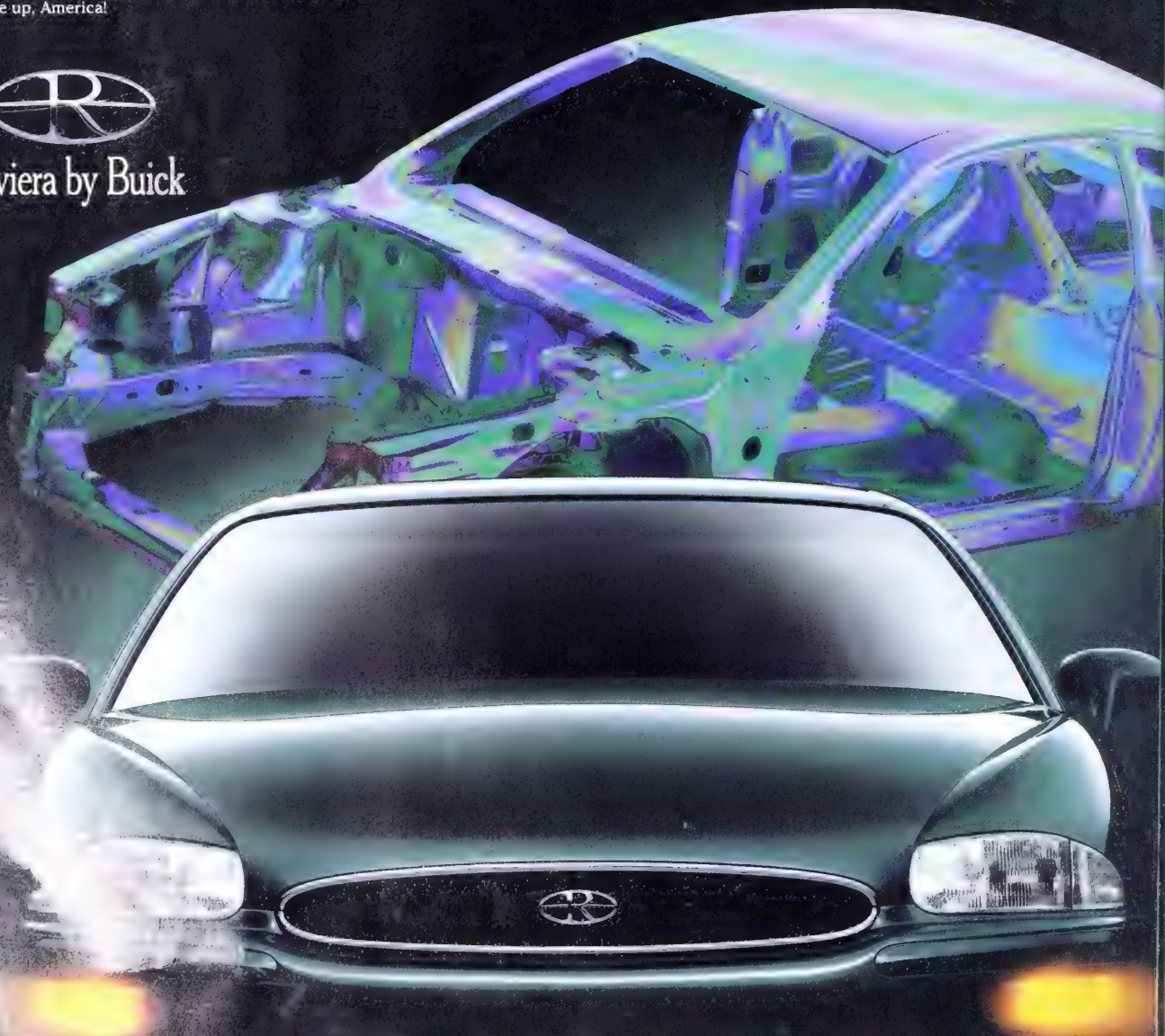
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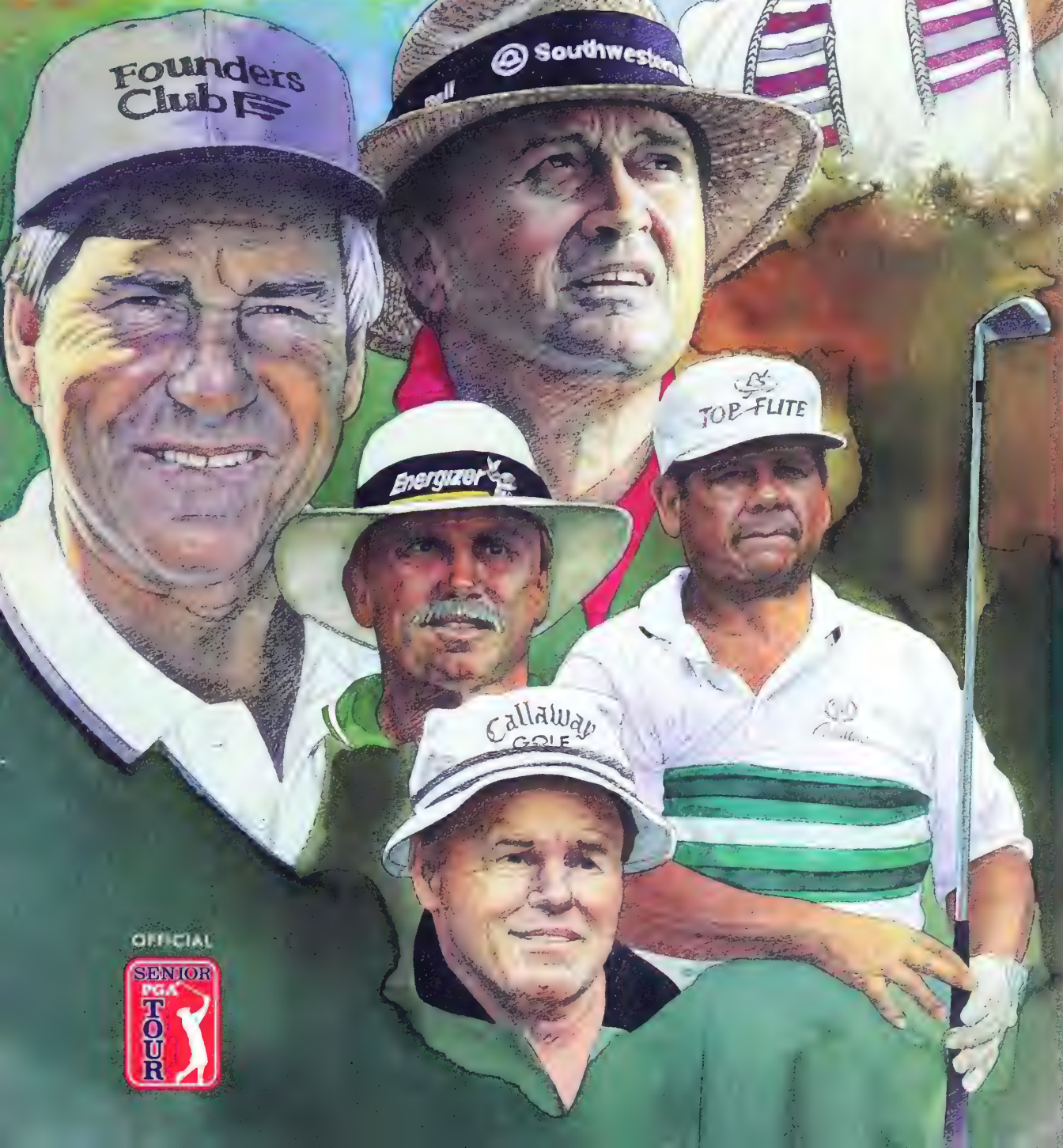


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Getting Ready for the Senior PGA TOUR

BY BOB VERDI

In professional athletics, expansion can be a polite synonym for dilution. More leagues mean more jobs on more teams, so it is only natural that demand for players will stretch supply to the outer limits.

Which is fine. Americans love their sports. Let the games grow on.

But the Senior PGA TOUR, unique in so many ways, again declares itself as different on the crucial matter of talent.

The Senior PGA TOUR debuted in 1980, staging two events for total prize money of \$250,000. In 1994, there were 44 tournaments for \$28,850,000.

Obviously, success of this enterprise is measured in quantum leaps. Yet, Dave Stockton, who won individual banking honors for the second consecutive season, can be assured that he will be challenged by a new and improved roster.

Which is as it should be. The list of fortysomething players who are ready, willing and able to join the fun and profit on the Senior PGA TOUR sooner rather than later is dazzling. The sport for ages 50-80 is still there to be seized at 50, that's where Hale Irwin will be on course. All he did in 1994 was finish second in wages on the PGA TOUR.



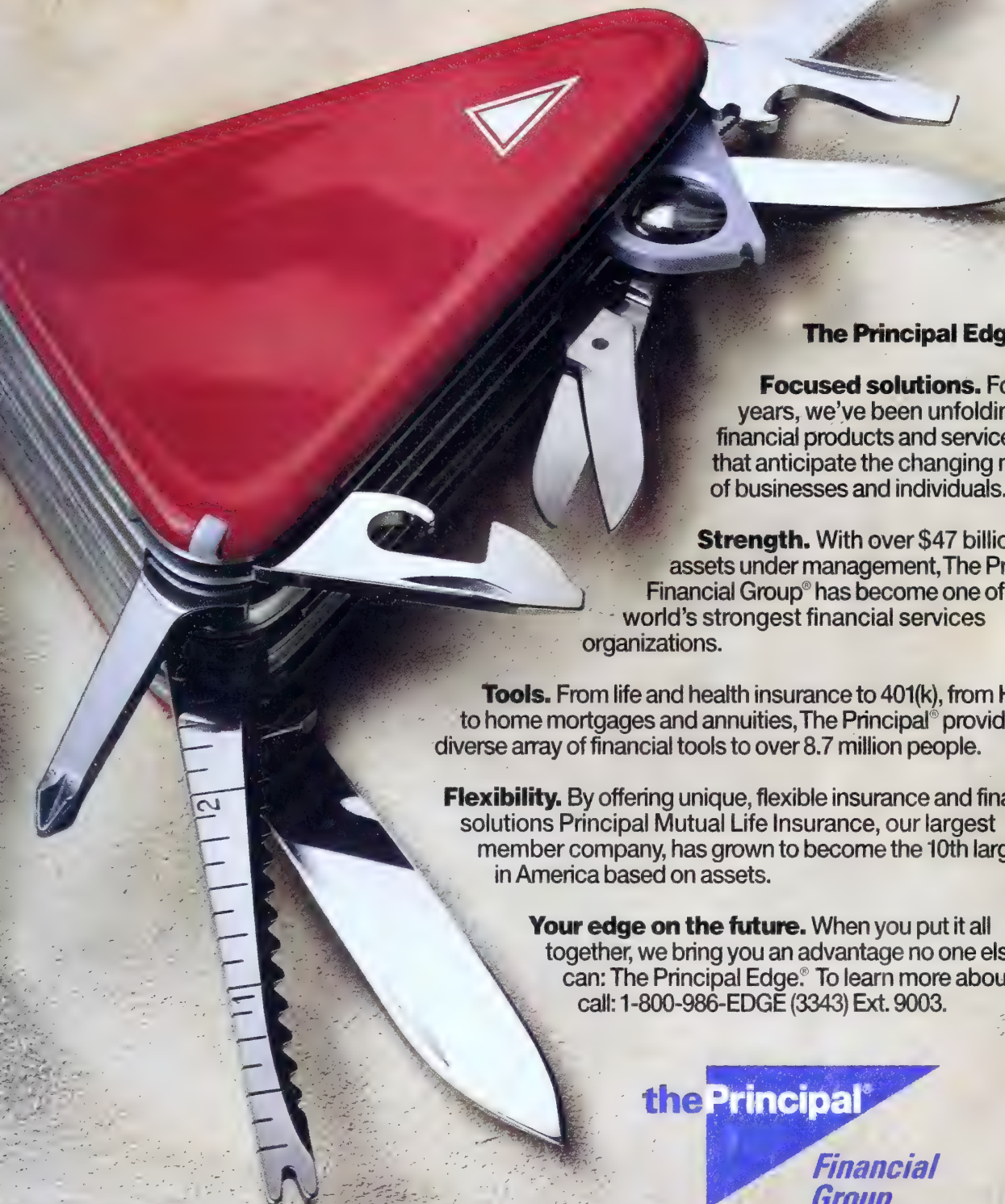
Older Presidents Cup captains: David Graham and Hale Irwin are both getting ready for the Senior TOUR

"Not too shabby," says Irwin, who did 91 holes of hard labor at Medinah Country Club in 1990, when he became the oldest winner (45) of a U.S. Open. That was his third such title for a machine man with a crowded trophy case, but cruise control is a gear the Irwin transmission doesn't include.

Example. Irwin knows the Senior PGA TOUR is out there. But so is the Ryder Cup. And he dearly wants to work for

a place on the United States team for the biennial matches at Oak Hill in Rochester, NY come September. Which is as it should be, again. Irwin is all about the zeal to compete, and that is the very essence of what energizes the Senior TOUR. "I'm sort of stuck, because of my birthday," Irwin said. "It comes right in the middle of the season. If I'm fortunate enough to be having any kind of a year on the TOUR, I'm sure I'll

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Practically/Amazing



nt to concentrate on getting enough
nts to qualify for the Ryder Cup."
When last seen in that grueling
urance test against Europe, Irwin
on the 18th green at Kiawah Island,
in September of 1989. His opponent
the 12th and final singles match was
rmany's Bernhard Langer, whose
t for victory missed. It was one of
se moments frozen in golf history.
"It was unbelievable, the pressure,"
in recalled. "I wouldn't have wished
t putt on anyone. But Bernhard

ne out of that fine, and
t's why we do what we
We love the game, we
e being in the hunt,
that's why the Senior
UR is so appealing. It
I always be there, and
be there before long."
So will David Graham,
Morgan and Hubert Green,
o turn 50 in 1996. To be followed by
nny Miller and Larry Nelson in
97. And how about this for the class
99? Tom Kite, Tom Watson and
ny Wadkins.

"David Graham, Tom Watson and
ere all in the same Q-school, the fall
1971," Wadkins mused. "Now, we're
sharpening up to get prepared for
Senior TOUR. How about that?"
"I know how old I am, so it's not
I'm sitting at home, crossing off
s on the calendar," Graham said.
at what I see and hear of the Senior
UR is phenomenal. I've basically
n inactive for the last four years.
ven't put my clubs in the closet.
on't have any banana-in-the-head-
er stories like Bruce Lietzke.

"But, I had a successful career on the
UR, I was personally satisfied, and I
nted to diversify my life, which I have
h the design company in which I'm
tners with Gary Panks. I met him

through Tom Weiskopf, and Tom is one
I keep in touch with. Everything he tells
me about his experiences on the Senior
PGA TOUR is terrific. He loves it. And
the lure of it to me is this: the one thing
I miss is getting up in the morning with
the challenge of being the best you can be.

"You have it occasionally in business,
but it's not quite the same. I've played
a lot of customer golf and I practice as
much as I can, but getting ready for the
Senior TOUR will require physical and

**"We love
the game, we love
being in the hunt, and
that's why the Senior
TOUR is so appealing,"
Irwin said. "It will always
be there, and I'll be
there before
long."**

skills, but, even after all those
years I traveled, I'll probably
have to learn how to pack
a suitcase again.

"I left the TOUR by
choice and I will go to
the Senior TOUR by
choice. I expect it will be
a real kick. And the other
bonus would be my sons, who
were too young when I was on the PGA
TOUR. One of the greatest things
I ever saw was that enormous bond
between Jack Nicklaus when he won



Tom Watson is preparing for his enrollment in the Senior TOUR's class of '99.



Tom Kite will be eligible to join the Senior TOUR in five years.

the 1986 Masters with (son) Jackie as
his caddie. That would be a treat, for
my Andrew or Michael to be there, now
that they've grown, if I happened to
win on the Senior TOUR."

"Just when you think you might
have had enough traveling, you see that
Senior TOUR out there. It's awfully
lucrative. There's no way to turn your
nose up at that, no matter how well
you've done financially. Plus, you get to
see new courses and old friends. That
sounds pretty tempting to me, not that
it's easy money by any means. Those
guys can flat play," Wadkins said.

For Kite, the PGA TOUR's all-time
money winner, a little extra cash would
be nice, if not necessary. But Kite, like
most of golf's upper echelon, operates
by a different standard. The ultimate
prize is triumph instead of a paycheck,
and the price you pay is that of com-
mitment and sacrifice. The notion
of the Senior PGA TOUR as this vast
Horn of Plenty cannot enter his
thoughts, at least now.

"I don't believe in comfort zones,"
Kite said. "If I allow myself to think
about all that might await me when I
turn 50, it would take away from what
I'm trying to do right now. If I wanted a
comfort zone, I wouldn't be on the PGA
TOUR to start with. And I've got five
years left before I have the choice anyway.

"People say I'm hard working, and

that's what I intend to be. I've worked at my game since I was a kid, and will continue to. I may hit the wall someday soon and not be able to get up over it again. I don't foresee that happening. I enjoy everything about the TOUR, and when the time comes, I'll probably be gung-ho for the Senior TOUR. Then, when I'm 53, the kids will be off to college, and it'll be just (wife) Christy and myself again, maybe just like starting out again on the Senior TOUR the way Dave and Kathy Stockton are doing it."

And, about that time, there will be another Texan to reckon with out on Golden Pond. Ben Crenshaw hits 50 in January of 2002 and if the sun is still shining, he'll still be making those putts from everywhere, just like Stockton.

"Hopefully," said Gentle Ben. "I've been very fortunate with that short stick, and no matter where you're playing, you still have to get the ball in the hole. There's also no substitute for the competition. I'm sure whoever you talk to

says the same thing. (They do.)

It's the competition and the camaraderie. The Senior TOUR has just catapulted. It's amazing. There's a lot of history out there. And the possibility of being part of it... going up against Tom Wastson and Hale Irwin and all those guys again on the Senior TOUR... well, that could be something. How could you not think about gearing up for that?"

Yes, but what about those gobs of money out there, fellas?

"It's significant," Irwin said. "But, again, I go back to the Ryder

**"Hopefully,"
said Gentle Ben.
"I've been very
fortunate with that
short stick, and no
matter where you're
playing, you still have
to get the ball in
the hole."**

Cup. There isn't money attached to it, but guys kill to get on the team. It's about pride, and it's about performance. The Presidents Cup (he was playing captain) got me excited all over again about that

type of competition. Competing against the younger guns out there keeps me young. There will be a time for an attitude adjustment, though, and I won't linger. Nor will I go to the Senior PGA TOUR just for the obvious rewards. I feel some responsibility to the sport of golf to play as long as I'm playing reasonably well."

Graham, meanwhile, recalls when picking one's spots wasn't an option.

"If you've been around like a lot of us, you remember when it wasn't so cushy," he said. "I won the Cleveland Open in 1972, and after I got paid, I still didn't have enough to buy the car I needed.



Julie Crenshaw with daughters Katherine and Clare look forward to watching Ben play golf as a senior

But that's good, because it makes you appreciate what we have in this game. We apply the rules of golf to the rules of life, and we've been fortunate to have people like Arnold Palmer, Jack Nicklaus, Sam Snead... on and on... such solid leaders.

"And that is very much a reason why we have what we have today. The Senior PGA TOUR has evolved from just something to do after you're 50 into the second most popular arena in golf. You have Nicklaus and Trevino and Player still out there, plus other players playing better than ever, plus a few new names like Jim Albus. It's really wonderful, and maybe I'm downplaying my anxiety to join them because it's still a little ways off.

"But it's quite the phenomenon. Golfers are in better shape than ever, approaching the game more professionally than ever, and the image of the sport has never been better. We've got this wonderful foundation and don't forget, the caliber of golf on the Senior PGA TOUR is excellent. If they couldn't still play well out there, it wouldn't have gotten where it is because of nostalgia." ▲



Ben Crenshaw is seen here competing on the Senior TOUR

'Friendly'

Johnny Miller talks about his Big Bertha Irons.



I've been playing with the Big Bertha Irons for a year now, and I would like to talk to you about a few important observations that I have made about these unique clubs."

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- Paul Azinger

"Higher trajectories really stop the ball on the green."

- Fulton Allem

"They'll put the iron play back in your game."

- Jim Colbert

"So easy to use."

- Chi Chi Rodriguez

"They're confidence builders."

- Patty Sheehan

"Gracefully muscular and solid."

- Bob Murphy

"They're in my bag -- to stay."

- Jim Dent

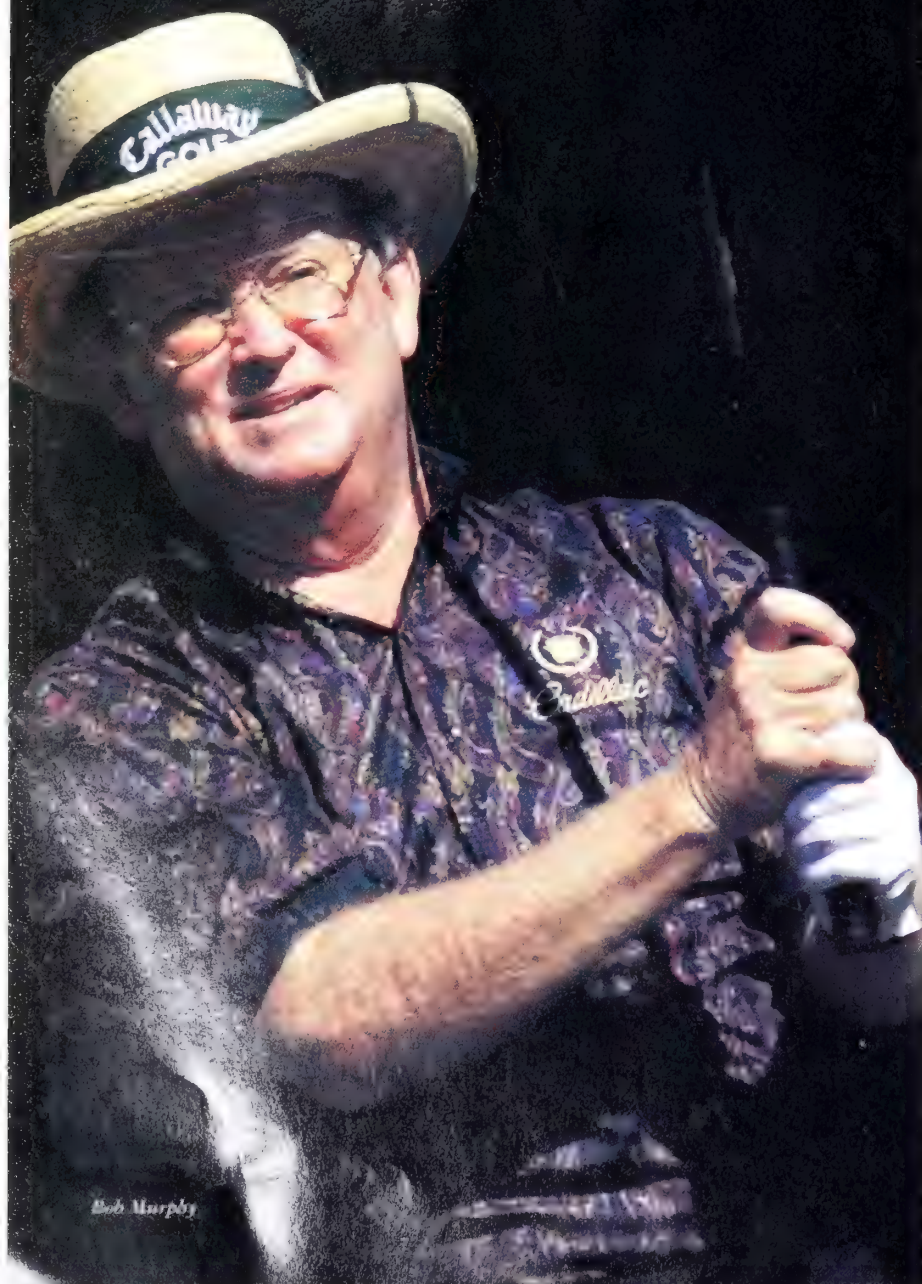


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The Good Old Days



Bob Murphy

BY RON GREEN

When a Senior PGA TOUR player arrived at a tournament and his luggage didn't, Margaret Lewis, the TOUR's director of travel, went out and bought him some shoes, socks and shaving equipment.

"I didn't have to," said Lewis, "but the motherly instinct comes out in me."

That's an instinct shared by people wherever the venerables tee up. Everything from courtesy cars to day care, from hotels to haircuts, is arranged for the players by the Senior PGA TOUR, sponsors, host cities, host clubs and assorted other benefactors.

When Lee Trevino or Walt Zembriski or Ben Smith show up to play, it's like a surgeon walking into an operating room. Somebody holds the gloves and gown and then hands them the scalpel.

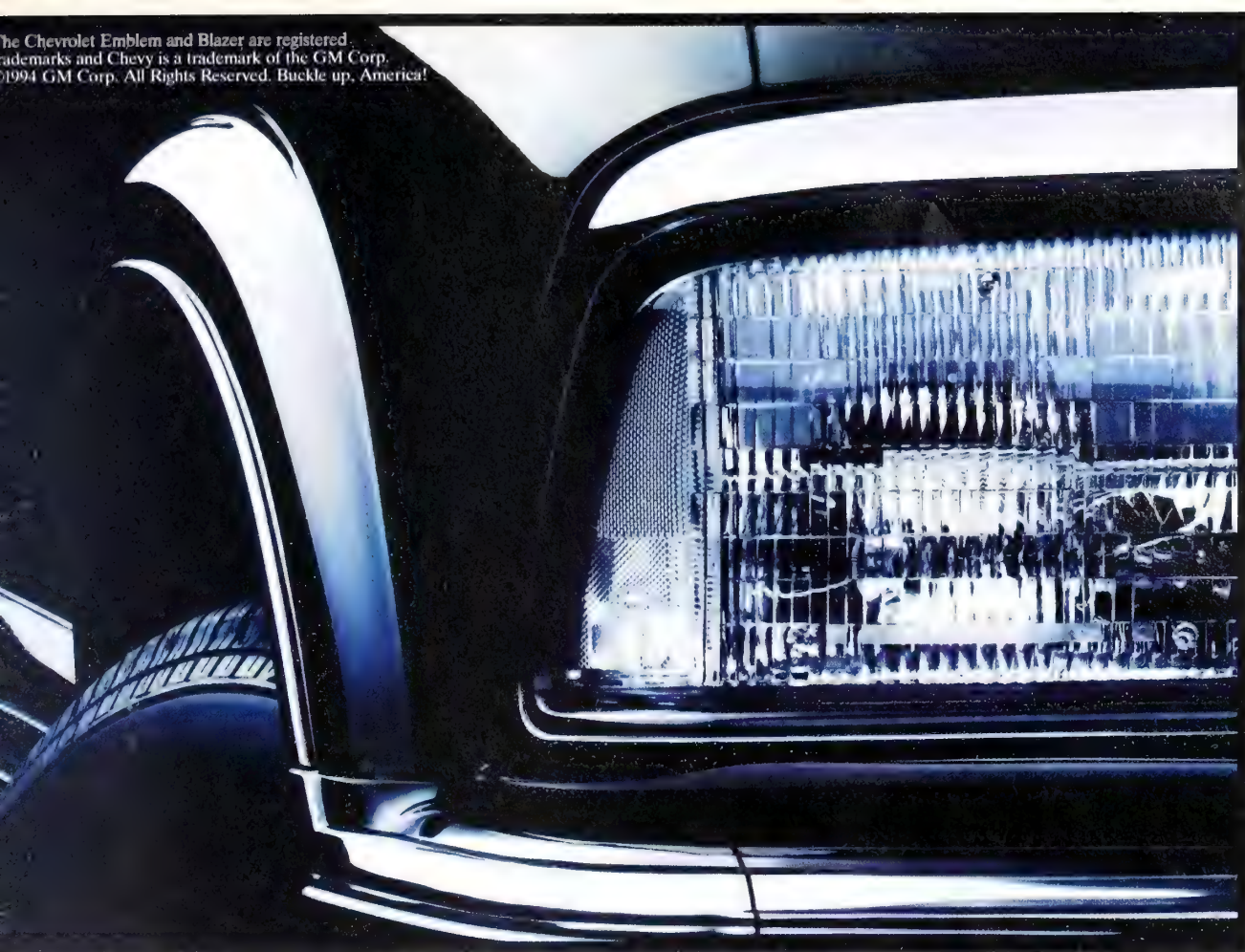
Bob Murphy, who won twice on the Senior PGA TOUR in 1994, says "Yeah, we're spoiled, but golf is a huge business. It's incumbent upon us to continue to look into how best to run the tournaments. You need things to run smoothly so the guys can stick to business instead of worrying about details."

But, Murphy points out, not everything is free, not everything is there at the end of the red carpet. The players ante up, too.

"It's a good life, if you're playing well," he said. "It's not if you aren't. Expenses are huge. You really need to make some nice money. A guy making \$150,000 is not doing very well. It costs you \$2,000 to \$2,500 a week minimum, and if your wife is with you, it's far more than that."

As the Senior PGA TOUR has grown, comfort and convenience have increased. Not the least of these, and reflective of the lifestyle these tournaments offer, is a Cadillac courtesy car provided every fully exempt player,

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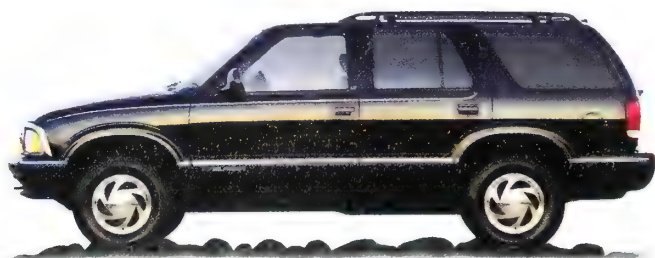
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d often more players, at
ch tournament.

"Good gracious," says
Miller Barber, remembering
w it was when he was
uffling around the TOUR
ck in the 1960s, "who
ould ever have thought
'd have a Cadillac car to
ive around?"

Good gracious, who would
er have thought the seniors
ould have child care? Or
ed it?

Lee Trevino, Larry Laoretti, Jim Ferree,
Geiberger and Tony Jacklin have
d the need for the child care service.
me tournaments even provide moms
th beepers, in case there is a need to
mmon them from the golf course.

Who would have thought one tour-
ment would pick up the players' dry
aning bills, another would provide a
cker room barber? Different locales
er different perks.

All have shiny new Titleist practice
lls. When the TOUR leaves town,
e balls are donated to junior golf.
All of them have telephone service in
e locker rooms, thanks to AT&T.

And the players can get all the tickets
ey need.

Locker rooms come in all sizes, shapes



Cadillac courtesy cars are provided to every fully exempt player on the Senior PGA TOUR.

and degrees of luxury. There is someone
there to gather up shoes, shine them and
return them to their lockers. There is
at least one host there to make certain
the players' needs are met.

There is also a private room
for the players' families.

Lunch is always free for the
players. Some tournaments
go well beyond that, though.
At the GOLF MAGAZINE
SENIOR TOUR Championship
in Myrtle Beach, SC, three meals
were served every day. A chef
was on hand to cook omelettes
to order in the morning in a
room adjacent to the locker
room. In the evening, The Dunes Golf
& Beach Club offered players and

their families four-course
meals, everything from
beef Wellington to roast
duck, except on Wednesday
and Thursday nights.

On Wednesday night,
the players were invited to
a pro-am pairings party and
on Thursday night, they
were free to attend the pro-
am awards dinner.

And on Saturday night,
they had tickets to see the
"Alabama" musical group

at a local theater. Entertainment is
available to them at every stop.

"They go out of their way to do
everything for us," said Donna Archer,
George's wife. "They treat us like visit-
ing royalty. Each tournament does
something different. It might be a lun-
cheon, fashion show, historical tour.

"My personal favorite is going to
baseball games. We also get basketball
tickets. They are always really good
seats. Sometimes we sit in the owner's
box at baseball games.

"I don't think there's a better life.
How could there be? We've had a blast.
"Most players won't take advantage of
entertainment options on days or nights
before they play the next day, preserving
their strength and getting plenty of



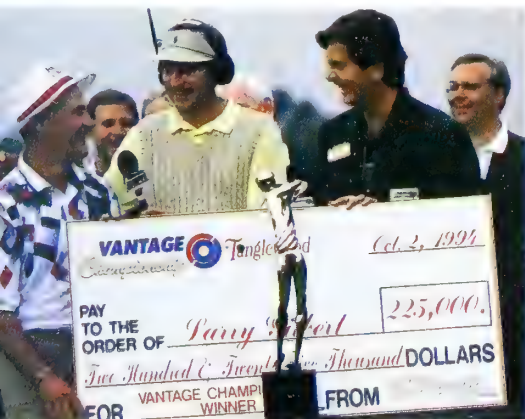
Each week, equipment repair trucks are on site to help the players.

rest. Many of them will go out to dinner,
though, rather than have room service.

Health is of utmost concern in tour-
nament golf. No play, no pay.

Sponsors make local doctors available
to the players. The TOUR also has two
doctors of its own, Dr. Frank Jobe and
Dr. Lewis Yocum, who visit the players
four or five times a year to evaluate
their health and offer advice. A chiro-
practor is also available periodically.

But the most important health benefit
the players have is a Centinela Hospital
fitness center, housed in a tractor trail-
er, at every site. They offer treatment,
exercise, cardiovascular exercise, strength



Many players have made more money in senior golf than they did on the PGA TOUR.

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Each tournament offers different amenities to make it easier for the players to concentrate on golf.

training and stretching programs.

It is manned by two physical therapists and athletic trainers, who supervise exercise programs featuring equipment such as bikes, treadmills, stair climbers, free weights and weight machines and treat players' aches and pains. They will see 30 to 40 golfers a day.

"That health van is a helluva perk for the TOUR," said Don January. "Mike Hill (who has won close to \$5 million on the Senior PGA TOUR) is a wonderful player because that thing loosened him up. His swing was too short and the therapists loosened his muscles so he could make a longer swing and now, you need a seat belt to play with him when he's hot."

One survey of the players showed that the Centinela fitness center was No. 1 on their list of favorite amenities.

One that is gaining popularity fast is the PGA TOUR's travel service. Three years ago, only 20% of the players used it. Now more than half do. Its primary function is to make airline, hotel and auto reservations for the players, at reduced rates. There are eight people working in the program. There is always one representative on site at PGA TOUR events and that may eventually extend to the Senior PGA TOUR.

The PGA TOUR offers an insurance program, which is essentially like the average

person's program, and a retirement program with benefits based on performance in tournaments. Occasionally, a Merrill-Lynch representative will drop by to answer players' questions about investing, although most players have their own financial advisors.

On the course, there is usually bottled water, Gatorade, fruit and candy. Before they go out, players are given sheets showing the exact location of the pins. Caddies are provided uniforms. Effort is made to have every course in peak condition. Electronic scoreboards around the course keep players and spectators informed of how the tournament is progressing.

"We're spoiled rotten," says January. "You've got all these companies trying to give things away."

And you've got all these sponsors trying to give money away. When January won the Atlantic City Senior

Invitational in 1980, the first year of the Senior PGA TOUR, there were only two events on the schedule, with a total purse of \$300,000. In 1994, there was about \$30 million in prize money. Six players won over \$1 million and 17 others won more than half a million. Every player in the GOLF MAGAZINE SENIOR TOUR Championship but Raymond Floyd had won more money in senior golf than they did on the PGA TOUR.

Henry Hughes, vice president and executive director of championship management for several PGA TOUR and Senior PGA TOUR events, said the benefits beyond the prize money are not demanded by the players.

"It's not so much that it's expected as it is that tournaments are happy to provide them," said Hughes. "They want to make it as easy as they can for the players to play and enjoy memories from that town. The players' job is to come and play golf and we try to make it easier for them to concentrate on that."

All those amenities just look free, of course. Ray Floyd and Jim Albus and Dave Stockton and the rest of them pay for them with their clubs. Still it's nice, when you're bending over a downhill, sidehill three-footer with a Stimp reading of about 25, if you aren't wondering about groceries or laundry. ▲



Today, cell phones and beepers are used by many players so they can be easily reached when on the course.

phones and beepers are used by many players so they can be easily reached when on the course.

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Jim Colbert



Jim Dent



George Archer

The Drive with a Difference

BY JACK BERRY

How is this for a sales staff? Arnold Palmer. Lee Trevino. Dave Stockton. Jim Colbert. Bob Murphy. They're all members of Team Cadillac, along with George Archer, Don Bies, Bob Charles, Dale Douglass, Harold Henning, Gene Littler, Bobby Nichols and Larry Ziegler.

Creating a Higher Standard is Cadillac's trademarked sales pitch and the luxury carmaker would be hard-pressed to create a higher standard than it already has in its golf program with the Senior PGA TOUR.

"It's a marketer's dream," said Alex Morton, executive vice president of D'Arcy, Masius, Benton & Bowles,

and lead man on the Cadillac Motor Car account. "And the results speak for themselves."

Cadillac's goal is to identify the prospect, find out what the prospect's "passionate interest" is and leverage it into a sale. And the Senior PGA TOUR demographics are a perfect fit with prospective Cadillac buyers.

Morton said Cadillac directly attributes more than \$250 million in sales to an association with the Senior PGA TOUR that began in 1990 with the 14 tournament Cadillac Series televised by cable sports network ESPN.

At the end of the 1996 season, 20 tournaments will be part of the series,

nearly half of the Senior PGA TOUR's official schedule. The continuity enables Cadillac to reinforce its message throughout the year.

PGA TOUR Commissioner Tim Finchem helped negotiate the original ESPN contract and said that when Cadillac signed on, Cadillac and ESPN asked the TOUR for a 5 to 7 p.m. air-time window whenever possible.

"Most PGA TOUR events conclude at 6 p.m. ET (on over-the-air networks) so Cadillac benefits with higher ratings in two ways with the 5-7 p.m. slot," Finchem said. "First, those fans interested in watching additional golf will change the channel to ESPN and follow the



PHOTOGRAPH BY JIMMY K. SMITH FOR THE SENIOR PGA TOUR

on the Senior PGA TOUR. And second, networks switch back to local affiliates for area news at 6 p.m., so Senior PGA TOUR golf on cable runs unopposed against any other sports event."

"Before the Cadillac Series began, the Senior TOUR had a lot of different time slots," said John Evenson, vice president, broadcasting for the PGA TOUR. "The Cadillac Series has established a viewing pattern — fans know the seniors will be on from 5 to 7 p.m. regardless of where the tournament is played."

"And it's three-day exposure," Evenson added, "Friday through Sunday. When the series started, we had about 100 hours of Senior TOUR golf on television, counting all networks. In 1995, it'll be in the 160-hour range with 130 hours on the Cadillac Series."

That exposure doesn't stop in the U. S., where viewership ranges from one million to a million and a half viewers. ESPN also distributes the shows to its international network and Senior PGA TOUR events also are aired in Japan.

A major component of the Cadillac Series drive is Team Cadillac, comprised of 13 leading players and headed by two of the most visible, popular names in all sport, Arnold Palmer and Lee Trevino.

Team Cadillac members have combined for 123 Senior PGA TOUR victories and 176 victories on the PGA TOUR, including 19 major championships. That's name recognition. They wear the Cadillac logo on their shirts so Cadillac usually is in the forefront at every tournament, not only in commercials, but during the play as well, and not just in the Cadillac Series events, but in every tournament.

"Team Cadillac provided us with credibility and visibility," Morton said. "It enabled us to align ourselves with golf much quicker without heavy promotional dollars."

All players collect points based on their money winnings in each Cadillac Series tournament. At the end of the year, the winner receives two cars, a Seville STS and a DeVille. The

runner-up receives an Eldorado Touring Coupe and the third place finisher a DeVille Concours.

Palmer never has cashed, as it were, but then he already is a partner with International Management Group President Mark McCormack in Cadillac dealerships in Charlotte, NC, and Arnie's hometown, Latrobe, PA. Palmer has been a Cadillac dealer for 15 years.

"I think it's fantastic what Cadillac has done with the car, particularly in recent years. I think everyone thinks of Cadillac as something they'd like to own and drive because it is such a nice luxury item," said Palmer.

"When Cadillac became an umbrella sponsor it gave more credibility to the Senior TOUR and it attracted other sponsors because they saw a quality company involved with us," Palmer added.



Cadillac has been the official car of the Senior PGA TOUR since 1990.



Dave Stockton and Lee Trevino are proud to be members of Team Cadillac.

Trevino was affiliated with a Japanese car (Toyota) before switching to Cadillac, and he has become a premier print and television spokesman.

"There was no question that Lee was going to be a major influence in senior golf," DMB&B's Morton said. "He's a perfect representative for Cadillac. He has a lot of charisma and he loves Cadillacs."

"They'd had Arnold all along — he's one of the biggest dealers in the country," Trevino said. "Arnold had handled (commercials) for quite a few years and they wanted someone to carry on. I started talking to them in 1990. I wanted to get with an American car and I was looking at Cadillac. I was going on the Senior TOUR full-bore to try and win as many titles and cars as I could."

"It was the best move for me career-wise and this car is second to none right now. You don't have to take it from me — look at Cadillac sales," Trevino said.

"Lee is a great salesman," DMB&B's Morton said. "You should see him go one-on-one with a prospect. I've had dinner with him at a restaurant and we've come out and someone is admiring the car and Lee goes into a sales pitch about the Northstar system. He gets in and takes 'em for a ride — you can ask for more than that from a celebrity spokesman. He knows everything about the car."

But Trevino likes the non-technical commercials he does.

"They tell a story. Like the first one I did when I said the closest I got to a Cadillac as a kid was when I was a caddy and took the clubs out of the trunk. We went from 'Is this a great country or what?!' to the one now about how everyone knows how I love to play golf and we bring in the Grand Canyon, Wall Street — I get a kick out of it."

"The primary Team Cadillac function is to wear the Cadillac shirt — anytime you get that logo on television it's worth very much," Trevino said. "And we drive the cars, do clinics, stop at the Cadillac tent at Cadillac Series events and say hello to dealers and customers."

Dealers invite prospects to tournaments, entertain them at the hospitality tent and sales are tracked by following up on those customers.

Corporate involvement in golf goes back decades and the demographics are a perfect fit for upscale carmakers. Buick was the first car company to put its name on a PGA TOUR tournament when it sponsored the Buick Open in 1958. Buick now has four PGA TOUR events. Oldsmobile, Chrysler, Lincoln Mercury, Honda, Nissan and Mercedes all have been involved with the men's and women's tours.

Cadillac long has supplied cars to the Masters Tournament, providing a fleet of white Cadillacs with the Augusta National Golf Club logo on the door for players and officials. Cadillac also provides cars at other tournaments and is the official car of the Senior PGA TOUR.

And if Cadillac is the official car, Team Cadillac's Dave Stockton may be the official clinician. The two-time

PGA Champion was the Senior PGA TOUR Player of the Year in 1993 and the first senior to put successive million dollar seasons together (1993-94).

Stockton has been a favorite of corporate America since his early days on the PGA TOUR when he developed a talent for the Monday and Tuesday outings where he'd give a clinic and talk golf with company officers and customers.

Captaining the 1991 team that regained the Ryder Cup for America put Stockton's name back in the consciousness of the golfing public and gave him a tremendous sendoff to the Senior PGA TOUR.

Jim Colbert and Bob Murphy, who were ESPN walking reporters, before joining the Senior PGA TOUR, are as handy with words as with their clubs and are accomplished clinicians.



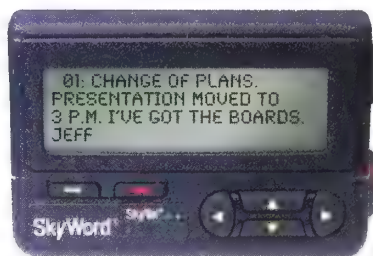
Cadillacs are popular with golf fans and \$250 million in sales prove it.

"They're all premier players and great gentlemen, and they're all good in their own right," Morton said. "We're developing video golf tips and vignettes with them and are looking to expand that and make clinic tapes."

And, looking at the young affluent market, Cadillac signed PGA TOUR star Fred Couples. For those long drives, obviously. 🏌️



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**They Walk
Softly and
Carry Some**

Big Sticks

BY LEW FISHMAN

A quick scan of the final statistics from the Senior PGA TOUR reveals some incredible numbers, not the least of which reside in the category of driving distance. Think for a moment of the stereotypical golfer who has passed his 50th birthday and then attempt to explain how the top ten seniors can average 264 yards or better on their tee shots.

Certainly, for some six-foot, 200-pounders such as Jim Dent, Tom Weiskopf and J.C. Snead, the answer lies in their physical size and strength. But for a growing number of senior pros, including those of slighter stature, the eternal quest for distance has routed them toward drivers that look more like fishing poles and behave more like slingshots. That's right, inordinately long drivers have elevated the likes of Rocky Thompson (267.8 yards), Terry Dill (271.7 yards) and Bob Carson (266.3 yards) into the Top Ten in driving distance and made them competitive in the senior circuit.

It seems ironic that the Senior PGA TOUR is acting as the incubator for such technology in golf equipment, particularly in light of the fact that 20 years ago these same golfers were hardly known for being particularly adept at swinging the club in their bag—and

preferring the tried and traditional.

And unlike the move to long putters, which has slowed, suffering somewhat from the stigma of having to use a "crutch" to overcome a bad stroke or the yips, indications are that long drivers will find their way into many more bags this year as a healthy number of pros have worked with them in the off-season.

"Just a few years ago, the standard driver length on the Senior PGA TOUR was 43.5 inches. Then it was 44 inches. Now, I would say it is 45 inches, and I have had a lot of requests for Big Bertha WarBirds that are even longer," said David Cagle, Callaway Golf's representative on the more mature TOUR.

The key to the long driver's distance potential is quite simple in that it allows golfers of average size to expand the arcs of their swings and create a

significant increase in centrifugal force, translating into clubhead speed through the impact zone.

Although clubmakers were aware years ago that ultra-long clubs would result in more distance, they had no idea that drivers of this type would allow golfers to hit the ball from one zip code into another. Nor did they have the capabilities of making such equipment, because steel shafts were too heavy to allow for such lengths and early graphite shafts possessed too much torque. Only after composite shaft manufacturers were able to rectify their problems in the mid to late '80s, using expensive ultra high modulus (stiffer) graphite to reduce torque and in some instances incorporating boron to add strength, did the extra-long driver become a viable entity. These advances and refinements in graphite technology allow Rocky Thompson, for example, to swing a 52-1/4 inch driver that weighs less than a 43-inch steel-shafted club.



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Because these days, organizations

that don't transform are likely to end up in the soup.

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For some seniors the extra-long driver offers the opportunity to regain the grace of their youth, but for the 1, 172-pound Thompson it is much more than that. "I was always a short hitter," he says. At the University of Houston in 1957, I was one of the shorter players, and later on the PGA TOUR I was without a doubt the shortest, hitting the ball only 235 yards off the tee on some of the softer courses. Everyone, including myself, thought this title belonged to Gene Beman, but I found out differently when I was paired with him in the Robinson Open in Robinson, IL. On my first tee, I 'clocked' my tee shot and

was feeling pretty good about it, knowing I was playing with the one guy I could outdrive. He got up, put that easy little swing on the ball and bunted it down the middle. We walked

"I will never hit the ball far enough to satisfy myself," says Thompson, who averaged 267.8 yards off the tee in 1994 and collected more than half a million dollars in official earnings.

down the fairway and darned if his ball wasn't five yards ahead of mine. And he did that to me all day, exactly five yards longer on every hole."

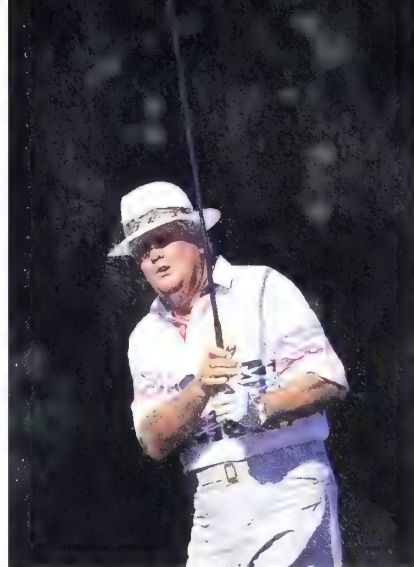
It's little wonder then that Rocky has a funny smile plastered on his face when he speaks of carrying the ball 280 yards, registering drives of more than 300 yards, and being asked not to hit drivers on the practice tee as he was at Kaanapali last year because the host club was afraid it would lose too many

golf balls when he popped them over the fence.

"I will never hit the ball far enough to satisfy myself," says Thompson, who averaged 267.8 yards off the tee in 1994 and collected more than half a million dollars in official earnings. "When you were the shortest hitter on the TOUR, you will do anything to become the longest, and I mean the absolute longest," he says sincerely, admitting to the fact that he has been working with a 54-inch "war club" that will allow him to gain still a few more yards.

Thompson, who turned to the long driver more than five years ago

Long drivers are found in the bags of many pros including Harold Hemming



Super Senior Gary Brewer uses long drivers to help improve his game.

when he assembled a 44.5-inch version in his home workshop, remains its staunchest proponent, spending more than \$20,000 on various shafts and clubheads. "I have built and hit more long drivers, worn out more clubs and caved in more clubfaces than any man alive. I am the King of the Driving Range," he says proudly, adding that his experimentation has led him to the ultimate realization of what works and what doesn't in these long clubs. His acumen will be put to the test this year when Thompson, the mayor of Toco, TX, unveils his own line of commercially-made woods and offers them to the public under the name Killer Bee.

Although not all of the Senior PGA TOUR pros using long drivers have made a science out of it the way Thompson has, they are no less enthusiastic about the prospects for the future. Furthermore, all of the players with whom we spoke thought this type of club had merit not only for the professional but also for serious amateur golfers willing to make a commitment, spend a few extra hours on the practice tee and incorporate a few adjustments into their swings.

"At first, amateurs probably are going to hit the long driver high and to the right, because they are working too hard trying to force the club into position. But if they stay with it, work with it on the practice range, they will find



PHOTOGRAPH BY GARY BROWN

that they will improve their tempo, and not only gain distance, but improve their accuracy as well," said Bob Carson, who credits his 46.5 inch driver for at least a few measured drives of 320-plus yards and some strong play in the last three Senior PGA TOUR events of 1994.

Carson, who contends he gained more than 30 yards on his tee shots since turning to the long club, also believes that the technique and tempo he implemented has helped his iron game dramatically.

Orville Moody, 1994's leading money winner among the Super Seniors (the 60 and over crowd) with \$208,490 in official earnings, echoes Carson's sentiments, stating that after being introduced to the long driver by Thompson six weeks before the end of the '94 season he began hitting the ball better than at any time during the last ten years.

The length of Moody's new driver, 49 inches, allows him to get the club to parallel at the top of the swing, something he had difficulty doing with the more traditional length club, he says, acknowledging a loss of flexibility.

Whether amateur golfers have the discipline and/or eye-hand coordination to control the ultra-long club at this time is purely a matter of speculation.

The 61-year-old former U.S. Open champion is looking forward to a big year in 1995, confident that he can consistently carry the ball 260-plus yards without sacrificing control or the ability to maneuver the ball. "I don't swing hard, just nice and

smooth, and I can feel the shaft do the work. The clubhead just seems to come into impact so square," Moody says with delight.

The "big stick" and its incremental distance benefit provides these talented professionals with the opportunity to hit shorter clubs on their approach shots to par 4s. It also allows them in some instances at least to reach par 5 holes in two with irons or more lofted fairway woods rather than having to hit driver from the fairway or play them as three-shot holes.

"I look at the long driver as shaving two shots a round from my score," says Homero Blancas, who catapulted up the money list last year with a 49-inch weapon in his arsenal. "Anytime you can go from hitting a 7-iron into a green to hitting a wedge, you are looking at a better score," he says, adding that the long club also has helped him to get a better trajectory on his shots. "I always had difficulty playing hilly golf courses because I hit a low, boring



Kevin Hagley of Brunswick Golf and Jim Dent admire the adjustments made to one of Jim's clubs at a tournament site.

shot that wouldn't carry very far. The extra-long, relatively flexible shaft in my driver now allows me to launch my shots higher and the ball carries farther."

To emphasize how much he believes this club has helped him, Blancas said that there were times last season when he hit 18 greens in regulation, a rare accomplishment even on the Senior PGA TOUR. "In bad weather at Indianapolis last year, I didn't miss a green for 36 holes. You can only do that when you are in good position off the tee," he says, a twinkle in his eyes.

Blancas believes, as do the others, that more golfers, professionals and amateurs, will adopt the longer driver in the near future. "It helps you do so many things right," he says. "The length of the driver and the quiet manner in which you must swing it helps your balance and makes it more difficult to move the club off-plane with your hands and arms," he reasons.

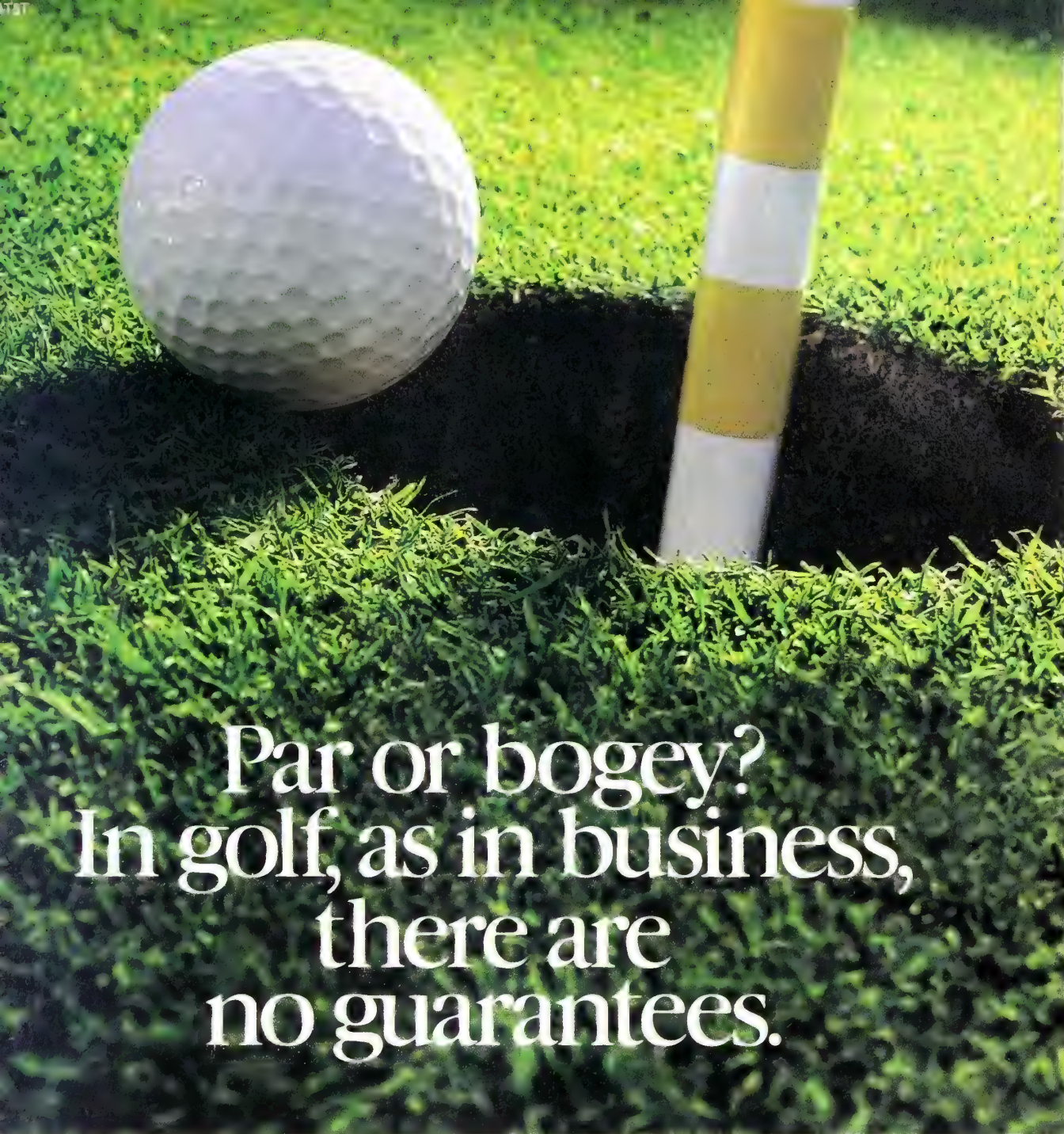
Whether amateur golfers have the discipline and/or eye-hand coordination to control the ultra-long club at this time is purely a matter of speculation. One thing is certain, however, and that is that the Senior PGA TOUR never will be the same, not when Rocky Thompson is outdriving Jack Nicklaus and loving every minute of it.

"It's like cheating," says Carson.

"It's like heaven," says Thompson. ▲



Rocky Thompson of the Dallas Cowboys turned to the long driver.



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Phil Stambaugh, Jr. with Jay Sigel

Jay Sigel knows a thing or two about amateur golf. He was one of the country's finest amateur players for almost 30 years. A graduate of Wake Forest University, Sigel won a British Amateur Championship in 1980, back-to-back U.S. Amateur titles in 1982 and 1983, and three U.S. Mid-Amateur titles in 1983, 1985 and 1987 – all while managing a successful insurance business in the Philadelphia area.

At the age of 50, he decided to take on the challenge of the Senior PGA TOUR.

After earning a conditional card at the National Qualifying School, Sigel won his first professional event in only his fourth start. In winning the GTE West Classic at Ojai, CA in a playoff, he completed the greatest comeback in Senior PGA TOUR history, rallying from 10 strokes behind by shooting a final-round 62.

Even though he had a list of impressive credentials before joining the circuit, Sigel realized he needed to improve his golf swing and hooked up with Mitchell Spearman, director of instruction for the David Leadbetter Golf Academy in Orlando, FL. Ironically, one of the few faults Spearman detected in Sigel's swing is something Jay observes too often while playing in mid-week pro-ams at Senior PGA TOUR events – the reverse pivot.

"The shot pattern I tend to see with most of my amateur partners is a ball that goes high, drifts to the right and lacks distance. It's a clear case of a reverse pivot. Either the weight stays on the left side throughout, or there is a weight shift back to the right but the lower body overturns," Sigel says.

Most amateurs know the golf swing requires a full shoulder turn, but they carry that thought all the way through into the

lower half of their body. In their mind, they believe they have made the proper full turn when, in fact, they have just twisted their torsos and kept all their weight on the LEFT side.

"What I strive to do on the practice tee is restrict my movement with my lower body. Believe it or not, when I do that correctly and make the proper turn, I not only hit the ball farther but with a great deal more accuracy, as well," he said.

Spearman developed an easy drill to help Sigel turn properly. It's one that will benefit players of all skill levels and can be incorporated into any practice routine.

The concept behind the exercise accomplishes three things: restricts the lower body, allows the hips to turn correctly and coils the shoulders fully into a powerful hitting position. It's important to remember that the "loading" of the right side occurs at the same time the golf club is moving into the backswing, and neither movement is independent of the other.

Lift the right heel off the ground during the setup and keep it off the ground as the club goes back, making sure the right leg remains flexed all the way to the top of the swing. From this position, the player should feel his weight shift from left to right and all the pressure move into the front of the right leg. "Lifting the heel should help to create some resistance between the upper and lower body in order to

build up torque and ultimately create additional clubhead speed," Spearman says. "It comes as a result of good leg action."

From a properly loaded right side, a player

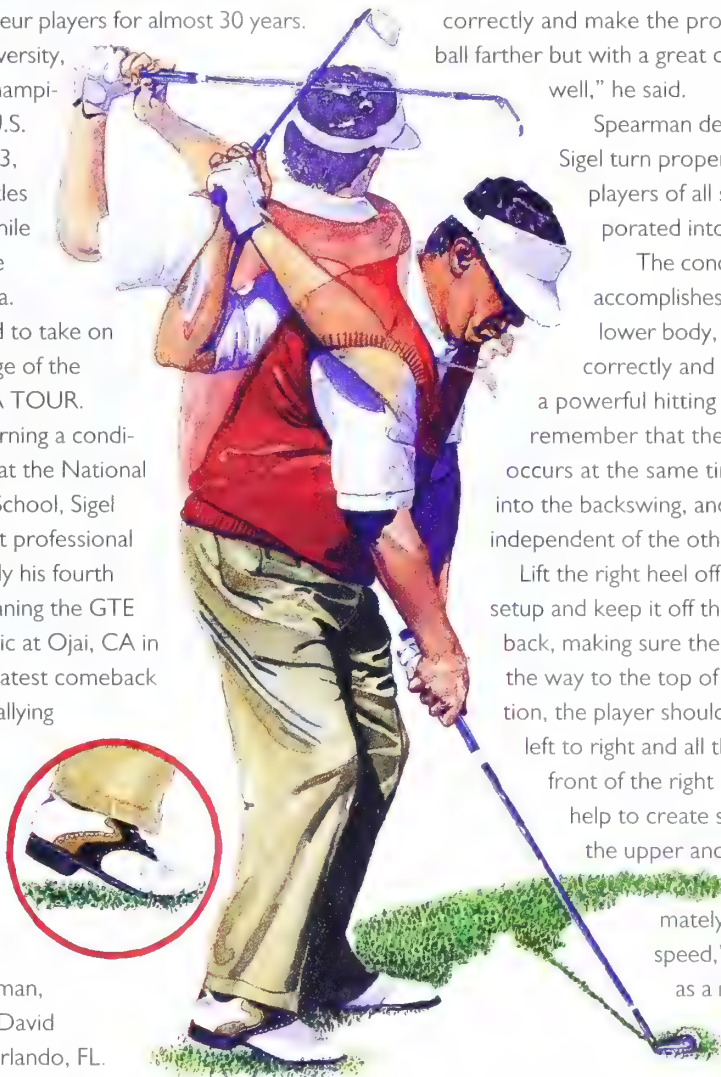
is now ready to release the club powerfully into the ball. Spearman again stresses the importance of feeling the pressure on the front of the right leg at the top of the swing. Lifting the right heel during the swing should produce the proper sensation.

"A good checkpoint is to examine the right knee during the swing," Spearman says. "If it moves backwards away from the ball at all, the hips have incorrectly overturned and the body is in the dreaded reverse-pivot position."

Repeating this drill correctly on the range should put players in a better overall position and will give them a pretty good chance of improving the quality of their shot. ▲



Jay Sigel



Impress Your Friends and Lower Your Scores

by Phil Stambaugh, Jr. with Jim Albus

The low-checking wedge is a shot that every professional has in his arsenal. When played correctly, it draws "oohs" and "aahs" from galleries at TOUR events almost every week.

To the average fan, seeing a ball come in low to a green at a high rate of speed, skip twice and stop quickly near the hole is a thing of beauty. People in the gallery at a tournament marvel at the skill of the shot-makers inside the ropes and may be jealous of a player's ability to pull this shot off with the wedge. They murmur to those fellow amateurs around them about the great feel required, the soft hands and deft touch it takes to save strokes from 50 yards or closer from the green.

What is perceived as being a difficult stroke to execute is, according to Jim Albus, actually fairly simple to learn. He believes it's really the only shot to play if you have plenty of green to work with, and one that should be incorporated into anyone's short game to lower their scores quickly.

Albus should know. Not only is he a former teaching professional at a prestigious New York country club, but is now recognized as one of the leading players on the Senior PGA TOUR. In 1994, Albus became the first former club professional to earn more than \$1 million in single-season earnings on the Senior PGA TOUR (\$1,237,128) and was tops in birdies with a record 453.

The former Metropolitan PGA Section Player of the Year captured the All-Around title, combining rankings from each of eight Senior PGA TOUR statistical categories. He also led the Senior PGA TOUR in posting rounds in the 60s with 54. Albus won the Vantage at The Dominion and the

Bank of Boston Senior Golf Classic tournaments last year, making him a multiple winner for the first time ever.

"The best part of this shot is that it's really the easiest way to hit a wedge, and there isn't a good player that I know that doesn't know how to hit it under the gun," Albus says. "There's a greater margin for error, and a punch wedge with a great deal of spin is the safest way out for a professional under a tremendous amount of tournament pressure."

Albus advocates three key points in learning how to hit the low spinner. First, make sure you have a sand wedge with a considerable amount of loft, 57 to 60 degrees preferably. Second, play the ball back in your stance. Way back, almost off your big toe. That will automatically deloft the club and give you the low flight you need.

"It's important to check and make sure the clubface is square or slightly closed. Too often, when you move the ball back in your stance, you open the clubface and that defeats the purpose of this shot," he says.

Finally, Albus emphasizes using a shoulder-dominated motion. He almost feels he is

"dragging" the arms and clubhead through the ball on the forward swing. It's definitely not a shot requiring any hand or wrist action. Just let the length of the shot dictate the length of the backswing and hit down and through, holding the clubface square as long as

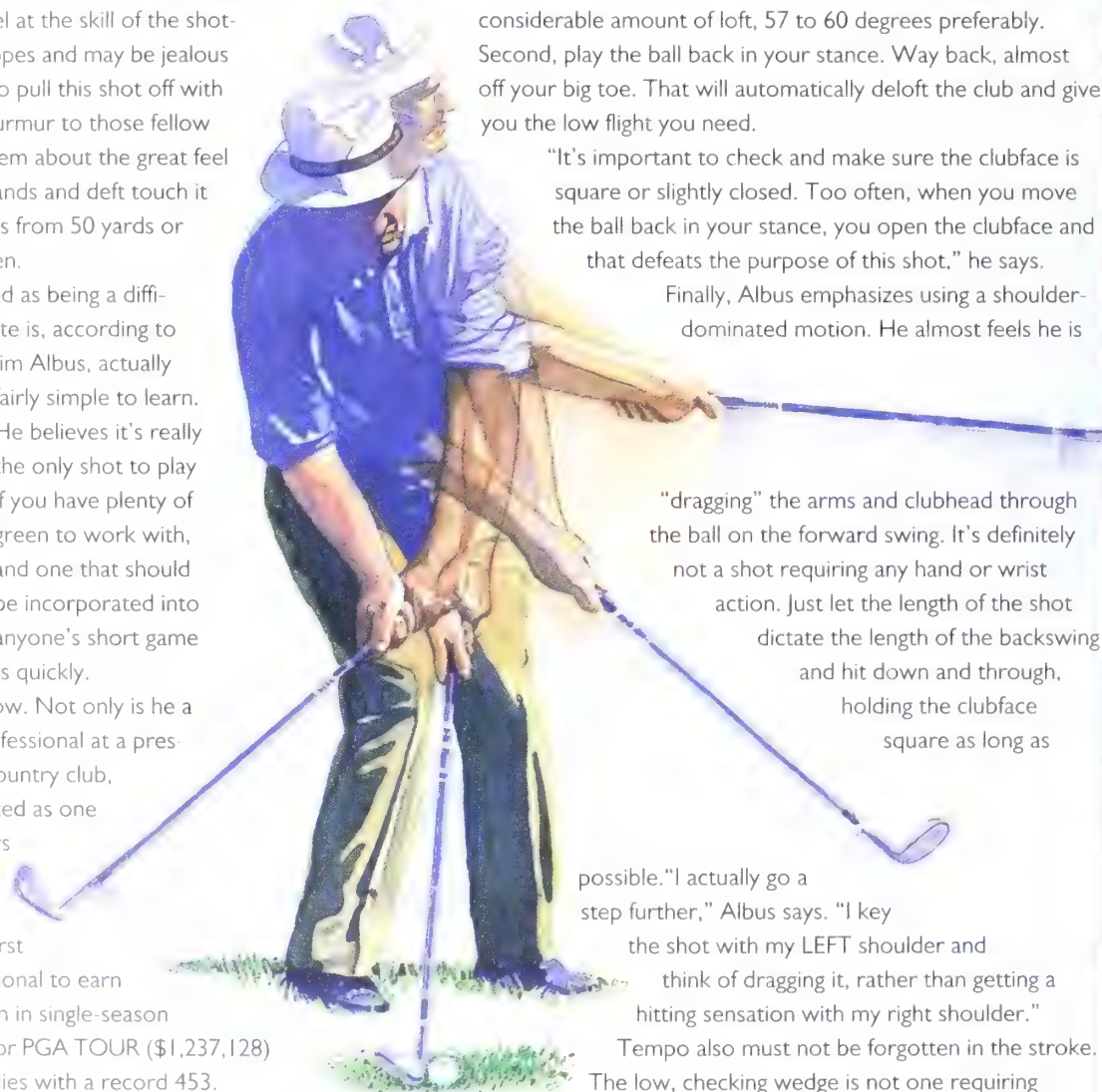
possible. "I actually go a step further," Albus says. "I key the shot with my LEFT shoulder and think of dragging it, rather than getting a hitting sensation with my right shoulder."

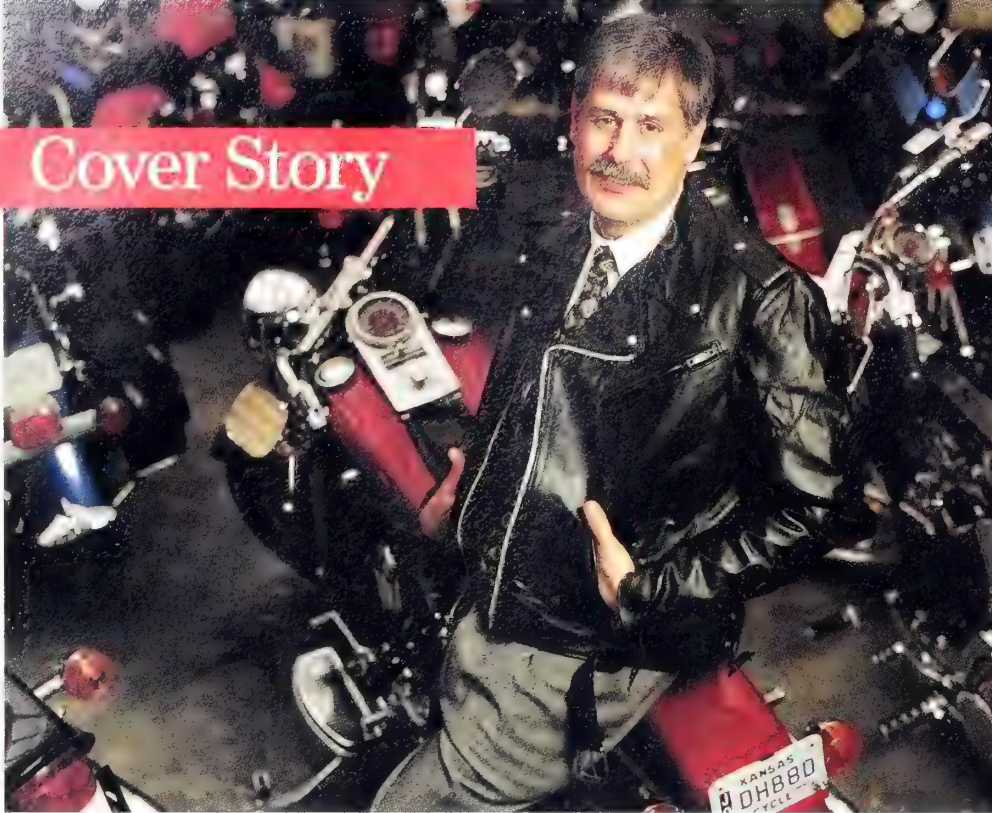
Tempo also must not be forgotten in the stroke. The low, checking wedge is not one requiring strength, rather finesse. You must maintain a smooth, lazy-ish, rhythmic motion throughout.

With a little practice, a shot you once thought was just reserved for TOUR professionals can now be used to lower your scores. And impress your fellow competitors.



Jim Albus





Cover Story

THE BEST MUTUAL FUNDS



All you need to know to find the ones that are best for you

Mutual-fund investors must be true believers. Even as stocks swung wildly last year, battered by the worst bond market since the Great Depression, investors in equity funds remained undaunted. Although cash inflows ebbed toward yearend, the final tally will likely be the second-highest on record. And 1995 is off to a strong start, too, says Robert Adler of AMG Data Services. Cash is coming into equity funds at the rate of \$2 billion a week.

Sure, 1994 was a dismal year for equity funds. The major stock indexes finished the year slightly on the plus side, but the average total return for equity funds was -1.8%, including dividends and capital gains. And that's before taxes, which could have eaten up an additional two percentage points.

Will equity-fund investors bolt, as some bond-fund investors

have already done? Not likely. Veteran mutual-fund analyst A. Michael Lipper of Lipper Analytical Services Inc. says investors need to amass capital to pay for college or retirement. "In the long run, these needs are better met with significant investment in equity funds" rather than fixed-income funds. Over the past five years, which include two down years, 1990 and 1994, funds still earned, on average, 9.1% a year. The 10-year average annual return—which includes the 1982 crash—is even better, 13.1% a year.

But that doesn't mean that investors will, or should, stay with the same funds year in, year out. Portfolio manager move on, investment policies change, fees rise. Or the investors' own objectives, preferences, and tax status change. And sometimes investors must switch because a fund just loses its way.

MARK SEFEROVICH

has owned his 10
gest holdings
ce 1990, and his
ted New
cepts earned a
ppy 11.3% in '94

clude detailed information on 885 equity
ds, 125 more than last year. Next week,
INNESS WEEK will publish expanded list-
s with 652 bond funds, many of which
ered large redemptions as investors
ned that bonds can be more risky than
ities. In two weeks, BW analyzes 260
ed-end funds, some of which are selling at
e discounts and offer juicy returns. The
reboard is compiled for BUSINESS WEEK by
ningstar Inc.

The equity-fund Scoreboard that begins
page 114 includes the critical data you



JAMES CRABBE
HARD HUSON

e buy stocks that
down 40% to
% over the last
months, and
re's no shortage
hose"

h the fund is sitting on.

And most important, we measure just how
ch risk the fund manager is taking. The
st Mutual Funds are not always the ones
t have posted the plumpest returns. The
t are those that have earned the highest reward for the
ount of risk they took with your money. That's why the
INNESS WEEK Scoreboard awards ratings to mutual funds
ed on their risk-adjusted total returns. And because fund
esting is a long-term proposition, we do not rate funds un-
they have logged a five-year track record.

This year, 47 funds earned three upward-pointing arrows,
highest rating, and they are a diverse lot (table). Some of
m, such as AIM Aggressive Growth, Hancock Special Equi-

That's where the
BUSINESS WEEK Mu-
tual Fund Score-
board can help you
plan your invest-
ments and monitor
just how your funds
are faring. This
year's Scoreboard
has been expanded

need to measure
mutual-fund perfor-
mance. For each
fund, we show total
return, both pre-
and aftertax, for the
past year and, de-
pending on their
history, 3-, 5-, and
10-year figures. We
compare a fund's
performance against
funds with similar
investment objec-
tives. We look at
the costs of buying
and remaining in-
vested in a fund.

RISKY? Then we
go inside each fund
to show how it in-
vests. We analyze
the "investment
style." Does it pur-
chase large-capital-
ization growth
stocks or small-cap
value stocks? Does
it buy stocks with
high price-to-earn-
ings ratios? We also
tell you how much

THE TOP PERFORMERS

These equity mutual funds have earned three upward-pointing arrows in the BUSINESS WEEK Mutual Fund Scoreboard. To get this rating, they needed to deliver superior risk-adjusted total returns over the last five years.

FUND	AVERAGE ANNUAL TOTAL RETURN*	INVESTMENT OBJECTIVE	RISK
AIM AGGRESSIVE GROWTH	23.5%	Maximum growth	High
ALLIANCE TECHNOLOGY A	22.0	Technology	Very high
CRABBE HUSON EQUITY	14.7	Growth	Low
CRABBE HUSON SPECIAL	19.5	Growth	High
EVERGREEN FOUNDATION	15.0	Balanced	Low
FAM VALUE	13.3	Small company	Low
FIDELITY ASSET MANAGER	11.1	Asset allocation	Very low
FIDELITY BLUE CHIP GROWTH	18.4	Growth	Low
FIDELITY CONTRAFUND	17.5	Growth	Low
FIDELITY LOW-PRICED STOCK	18.9	Small company	Low
FIDELITY SELECT C COMPUTERS	24.0	Technology	Very high
FIDELITY SELECT ELECTRONICS	23.1	Technology	High
FIDELITY SELECT HEALTH CARE	18.6	Health care	High
FIDELITY SELECT HOME FINANCE	23.6	Financial	High
FIDELITY SEL. SOFTWARE & COMP. SVCS.	21.6	Technology	Very high
FIDELITY SELECT TECHNOLOGY	22.3	Technology	High
FLEX-FUNDS MUIRFIELD	9.7	Asset allocation	Very low
FOUNDERS WORLDWIDE GROWTH	13.2	World	Low
GATEWAY INDEX PLUS	9.1	Growth/income	Very low
HANCOCK FREEDOM REGIONAL BANK B	18.2	Financial	Average
HANCOCK SPECIAL EQUITIES A	21.8	Small company	Very high
HEARTLAND VALUE	16.4	Small company	Average
INVESCO STRATEGIC FINANCIAL SRVCS.	18.0	Financial	High
INVESCO STRATEGIC LEISURE	16.7	Specialty	Average
INVESCO STRATEGIC TECHNOLOGY	22.5	Technology	High
KAUFMANN	19.3	Maximum growth	High
LINDNER DIVIDEND	9.9	Income	Very low
MERGER	9.4	Growth	Very low
MERIDIAN	16.6	Small company	Average
MERRILL LYNCH GLOBAL ALLOCATION B	10.7	Asset allocation	Very low
MFS EMERGING GROWTH B	21.4	Small company	Very high
MUTUAL BEACON	11.5	Growth/income	Very low
MUTUAL QUALIFIED	11.6	Growth/income	Low
OPPENHEIMER MAIN ST. INC. & GR. A	22.2	Growth/income	Average
PBHG GROWTH	22.0	Small company	Very high
PHOENIX CAPITAL APPRECIATION A	15.3	Growth	Low
PIMCO ADVISORS OPPORTUNITY C	21.0	Maximum growth	High
T. ROWE PRICE SCIENCE & TECHNOLOGY	22.0	Technology	Very high
SELIGMAN COMMUNICATIONS & INFO. A	24.2	Technology	Very high
SKYLINE SPECIAL EQUITIES	18.2	Small company	Average
SMITH BARNEY PREMIUM TOTAL RETURN B	11.1	Equity-income	Very low
SOGEN INTERNATIONAL	10.5	Asset allocation	Very low
STRONG COMMON STOCK	19.0	Small company	Average
UNITED NEW CONCEPTS	19.9	Small company	Average
VANGUARD SPECIAL HEALTH CARE	15.6	Health care	Average
VISTA GROWTH & INCOME A	14.9	Growth/income	Low
WARBURG PINCUS GROWTH & INCOME	13.6	Growth/income	Low

*1990-1994 pretax return, includes appreciation plus reinvestment of dividends and capital gains

DATA: MORNINGSTAR INC.

ties, PBHG Growth, and Seligman Communications & Information Fund take on high risk, buying the shares of rapidly growing companies at high p-e ratios.

That can lead to some wild rides. Just look at the Seligman fund, which specializes in technology stocks. The fund was the best performer both for 1994, up 35.3%, and for the five-year period, an average annual return of 24.2%. Yet it's not for the faint of heart. From March to June of last year, the fund lost 22% of its net asset value. But the beauty of the BW ratings

is that funds don't have to take high risks to win accolades. At the other end of the spectrum, there's Flex-funds Muirfield, Gateway Index Plus, Lindner Dividend, and Merger Funds. Each of these funds beat the market by a

Cover Story

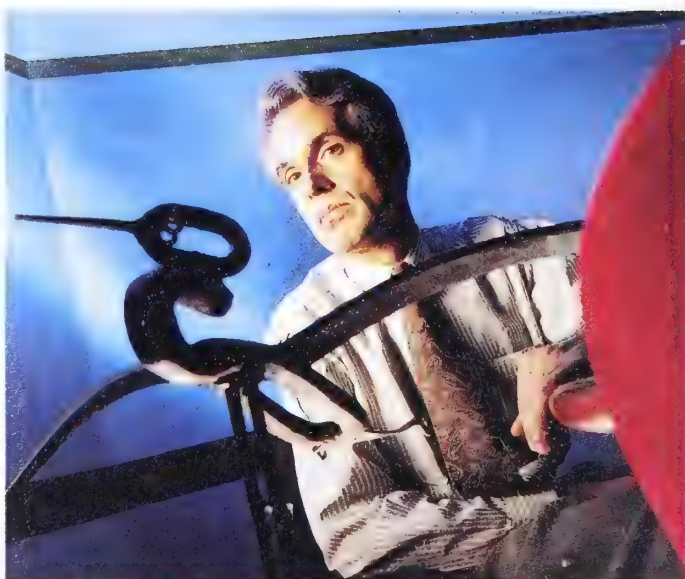
percentage point a year or less. That may not sound like much until you consider that the risk rating of each of these funds is "very low" and that of the stocks in the Standard & Poor's 500-stock index is "average." If a fund can deliver a little more return at a lot less risk, it's worth lauding. Such funds should appeal to investors who should be in equities but are reluctant to bear the day-to-day volatility of the stock market.

These top funds all take different approaches to investing. Lindner Dividend focuses on generating high yields and Gateway on selling options. Perhaps most unusual is Merger Fund, which, true to its name, invests in companies after a merger agreement is announced. The strategy is not without risk—deals after all do fall apart—but that risk is not correlated with that of stock market. "Strategic deals that make sense get done even in an unfavorable market," says Fred Green, who with Bonnie L. Smith manages the fund. Last year, the fund earned a 7.1% total return.

Not all of the top-rated funds beat the market during

ANTHONY ORPHANOS ►

His Walburg Pincus has been 40% in cash since Labor Day. He's in no hurry to spend it



THE LARGEST FUNDS

Here's the BUSINESS WEEK Mutual Fund Scoreboard rates the largest equity mutual funds:

FUND	ASSETS BILLIONS	BW RATING	AVG. AN'L TOTAL RET.*
FIDELITY MAGELLAN	\$36.4	▲	12.0%
INVESTMENT COMPANY OF AMERICA	19.3	AVG	8.8
WASHINGTON MUTUAL INVESTORS	12.7	AVG	8.0
FIDELITY PURITAN	11.8	▲▲	10.7
FIDELITY ASSET MANAGER	11.1	▲▲▲	11.1
VANGUARD WINDSOR	10.9	▼	8.6
INCOME FUND OF AMERICA	10.5	▲	8.4
TWENTIETH CENTURY ULTRA INVSTRS.	9.9	▲▲	19.4
JANUS	9.4	▲▲	10.7
FIDELITY GROWTH & INCOME	9.3	▲▲	12.5
VANGUARD INDEX 500	9.2	AVG	8.5
FIDELITY CONTRAFUND	8.7	▲▲▲	17.5
VANGUARD WELLINGTON	8.6	▲	7.9
EUROPACIFIC GROWTH	8.3	▲	10.7
VANGUARD WINDSOR II	7.9	AVG	7.8
FIDELITY EQUITY-INCOME	7.4	▲	9.2
DEAR WITTER DIVIDEND GROWTH	6.7	AVG	7.2
NEW TRASPECTIVE	6.5	▲	10.3
MERRILL LYNCH GLOBAL ALLOC. B	6.3	▲▲▲	10.7
T. ROWE PRICE INT'L. STOCK	6.0	▼	7.2

LEGEND: (▲) superior, (2 arrows up) very good, (1 arrow up) above average, (1 arrow down) below average, (1 arrow down) poor, (3 arrows down) very poor

SOURCE: INVESTMENT COMPANY INSTITUTE

1994. Most funds that held some bonds—mainly asset-allocation, balanced, and income funds—were pulled down by those holdings. But in 1993, they were golden as rates fell and bonds surged in value.

Although Merrill Lynch Global Allocation B Fund and Fidelity Asset Manager retain their top ratings, they failed to beat the S&P in 1994. Both funds have wide latitude to invest at home or abroad, yet neither came up with a winning mix.

The Merrill fund suffered a -2.9% return. The Fidelity fund, -6.6%, was dragged under by its holdings in emerging markets, a source of plump returns in previous years. "I was lowering emerging-markets holdings all year, but I didn't get to zero soon enough," says Robert A. Beckwith, who runs Fidelity Asset Manager. The fund is down 1.3% so far this year.

DEARY SHOWING. International investing lost most of its luster in 1994. About the only market to make gains was Japan's—and a scant few fund managers had invested there. And though the Mexican currency crisis that began in mid-December contributed to the dreary performance abroad, the international funds were not faring particularly well until then either. Even Founders Worldwide Growth Fund, the only world fund to get a top rating this year, recorded a -2.2% return in 1994. But fund investors have not lost their appetite for overseas investing. Last year, international funds took in 37% of the inflows to stock funds, according to Avi Nachmany of Strategic Insight Inc., a fund-industry consulting firm. But AMG's Adler senses a slowdown—so far this year only 10% of the new money is going global.

With jittery markets, it was no wonder fund managers had a tough time getting any positive results. But even funds with a bearish bent, such as the Robertson Stephens Contrarian Fund, fared no better. Anticipating higher inflation, the fund loaded up on gold, metals, and energy stocks and sold short popular highfliers, betting on a big market plunge. The fund had a 5.5% loss for the year.

"It was a year in which almost nothing worked," sighs Jean-Marie Eveillard, portfolio manager of the Sogen International Fund. "Even gold didn't pay out." Gold bullion and gold mining shares had soared in 1993, but in 1994, precious metals funds were the worst performers, down 9.2%. Eveillard managed to eke out a 2.5% total return for the year, mainly because of some shrewd stock picks and a pile of cash

funds that invested in low p-e and price-book stocks—so called “value” stocks—fared better in the first half of 1994. Those that bought higher p-e “growth” stocks did better in the second half. This reversal in the trend explains why, overall, the results of the various investment styles as shown on the 112 are not significantly different from one another. But investment style will make a difference this year. If the economy slows, as most expect, funds with a growth-stock tilt should do better. True “growth companies” don’t need a robust economy to generate profits.

As a matter of policy, many funds keep most of their money invested in stocks, not allowing cash to pile up. Those that could and did keep cash fared relatively strong in performance. Anthony G. Orphanos, portfolio manager of the top-rated Warburg Pincus Growth & Income Fund, up 7.6% in 1994, took profits in technology stocks during the summer and has had 10% of his fund’s assets in cash since September. Orphanos is in no hurry to spend it. To become bullish again, he needs, “I have to see evidence that the economy will slow precipitously or that long-term interest rates would have to fall below 7%.”

IT RIDE. Mark G. Seferovich, who manages the United New Concepts Fund, has his cash cushion, now 27%, helps dampen the swings inherent in portfolios of small-company stocks. And he doesn’t consider cash to be a drag during bull markets either. “In an up market, stock selection will overpower the weight of cash any day,” says Seferovich. He’s also happy to let his profits run. The 10 largest holdings, including motorcycle manufacturer Harley-David-

son Inc., have been in the fund since 1990. He earned a net return of 11.3% last year, and 19.9% over the past five years. That helped him win three up-arrows in the BW Scoreboard. At the Flex-funds Muirfield Fund, cash is not a cushion but a strategic weapon. Manager Robert S. Meeder Jr. moved to cash last March and stayed that way until yearend. Now, he has put most of that money back to work. The fund has 10% of its assets in equities—which in Muirfield’s case is in equity funds. Its largest holding is Fidelity Capital Appreciation Fund, 6% of assets. Others include Fidelity’s Blue Chip and Growth & Income funds, as well as Neuberger Berman Focus and T. Rowe Price New Horizons funds. About 20% of the fund is in 10-year U.S. Treasury bonds. Technology funds were the big winners in 1994—and so were those diversified funds that banked heavily on high tech, such as Fidelity Blue Chip Growth Fund. The entire sector of the market benefited from increased capital spending on productivity-saving technology and on the public’s

THE FUND GROUPS

Last year disappointed many fund investors—if only because the previous several years had been so strong. Technology funds were the standouts, while precious-metals funds, which nearly doubled in 1993, were 1994’s dogs.

FUND OBJECTIVE	TOTAL RETURN (PERCENT)*				BEST-PERFORMING FUND IN 1994
	1994	1992-94†	1990-94†	1985-94†	
TECHNOLOGY	13.1	17.4	19.0	15.5	Seligman Comm. & Inform. A
HEALTH CARE	5.3	-1.3	14.9	19.8	Fidelity Select Health Care
EUROPE	1.6	8.1	3.9	NA	Fidelity Europe Cap. Apprec.
SPECIALTY	0.9	12.2	10.7	19.9	Fidelity Select Chemicals
NATURAL RESOURCES	-0.1	8.8	5.4	10.3	Fidelity Sel. Paper & Forest
SMALL COMPANY	-0.3	9.6	12.4	13.5	PBHG Emerging Growth
GROWTH/INCOME	-0.6	7.0	8.7	12.8	Safeco Equity
GROWTH	-1.4	6.9	9.7	13.4	Montgomery Growth
FINANCIAL	-1.5	16.7	15.7	13.4	Fidelity Select Home Finance
EQUITY-INCOME	-1.6	7.7	8.1	11.8	Fidelity Adv. Equity Income A
MAXIMUM GROWTH	-2.1	7.3	12.3	14.5	AIM Aggressive Growth
ASSET ALLOCATION	-2.7	6.2	7.7	10.7	Quest For Value Opportunity A
BALANCED	-2.7	5.6	8.2	11.7	Dreyfus Balanced
WORLD	-2.8	7.9	6.1	14.0	Dean Witter Global Div. Grth.
FOREIGN	-3.8	10.1	6.4	15.8	New England Intl Equity A
INCOME	-4.4	6.2	8.3	10.7	Putnam Managed Income A
PACIFIC	-6.9	11.5	3.5	15.4	Fidelity Japan
UTILITIES	-8.5	5.0	6.6	12.5	Fidelity Select Telecommun.
PRECIOUS METALS	-9.2	11.7	0.3	6.1	Lexington Strategic Invstmnts.
U.S. DIVERSIFIED FUNDS	-1.0	7.5	10.0	13.3	
ALL EQUITY FUNDS	-1.8	7.8	9.1	13.1	
S&P 500	1.3	6.3	8.7	14.4	

*Pretax return, includes appreciation plus reinvestment of dividends and capital gains

†Average annual

NA=Not available

DATA: MORNINGSTAR INC

growing appetite for gadgetry such as PCs and cellular phones.

After four years of strong performance, can you still bet on technology? “Sure, we have a lot of technology,” admits Michael Gordon, Blue Chip’s manager. “But we talk to the companies all the time, the business prospects are great, and the stocks are not expensive based on their growth rates.”

Nonetheless, fund analysts generally warn investors not to chase the top-rated specialty funds such as the Fidelity Selects: Computers, Electronics, Software & Computer Services, and Technology. “Usually, the point at which everything looks great about a sector is the time you have to worry about getting out,” says Don Phillips, publisher of *Morningstar Mutual Funds*. Phillips suggests buying more diversified funds that can invest in technology and leaving the specific technology sectors to the portfolio manager’s expertise. The average growth fund already has 20% of its assets in technology, and some small-cap growth funds more than 30%.

Smart mutual-fund investing takes work. And the place to

Technology funds were big winners in 1994, as were diversified funds heavily invested in high tech

Cover Story



▲ BONNIE SMITH FRED GREEN

Their Merger Fund
invests in announced
deals and had a 7.1%
return in 1994

Next comes the 1994 returns, both pretax and aftertax. Yes, investors in mutual funds may still be stuck with a tax bill even if the fund didn't make any money during the year. Here's why: By law, the fund must dis-

tribute its net income—that shows up in the "yield" column—as well as any realized capital gains. So even if net asset value fell, there may be some taxes owed.

SHARP PAIN. Look at Twentieth Century Growth Investors on page 138. The pretax return for 1994 was -1.5%, a little better than the average equity fund. But this fund also made large capital-gain distributions amounting to about 15% of NAV. After taxes, the fund's return dropped to -5.6%. That would have been particularly painful to new investors in the fund, who didn't have their money invested long enough to take advantage of the portfolio's long-term gains. "It's like arriving at the party as it's breaking up and getting stuck with the caterer's bill," says Morningstar's Phillips.

Can you guard against being blindsided by large capital-gains distributions? Not entirely, but there are some tip-offs. Is the fund's asset base shrinking? You can tell that from the "% chg." column under

get started is the BUSINESS WEEK Scoreboard tables (page 114). The funds are listed alphabetically, and if they accumulated a five-year record, their BW rating follows the name. Also, be on the watch for a head-and-shoulders icon. The solid icon indicates a portfolio manager with 10 years at the helm. A head-and-shoulders outline means there's a new manager on the job.

MUSHROOM. The next column, "Assets," is the fund's size. Fidelity Magellan Fund notwithstanding, performance often slows as funds grow. Check out Crabbe Huson Equity and Crabbe Huson Special Funds on page 116. Both funds rate three up-arrows. Because of that performance, the Crabbe Huson Special Fund in particular has mushroomed—its assets were up 1,200% over the last year. Most of the fund's admirable record was amassed when it was a mere fraction of its current size.

Portfolio manager James E. Crabbe says neither the Special fund nor the Crabbe Huson Equity, run by partner Richard S. Huson, will have any trouble finding investment opportunities. "We buy stocks that are down 40% to 50% over the last 24 months, and there's no shortage of those," says Crabbe. The key, he adds, is to determine which of the depressed stocks can rebound in the next year or two. For instance, they started buying IBM at 46 when Big Blue was flat on its back. Today, it's at 74. Crabbe's next high-tech comeback bet is Cray Research Inc., down from 50 to 15. His firm holds 5% of the company and believes it's at least a double.

Moving to your right along the Scoreboard, you'll find fees, both sales charges—often called "loads"—and expense ratios, which is the annual cost of keeping your money in the funds. The average expense ratio is 1.29%, or \$1.29 for every \$100 in the fund. The higher the expenses, the more it eats into your returns. And that's a cost to be borne whether or not the fund makes money.

assets. That could mean more money is coming out than going in, and managers may have to cash in some winners to meet redemptions. A new portfolio manager may also offer a clue. He may sell stocks—and unlock unrealized gains—to recast the portfolio to his own liking. Are there unrealized gains in the fund? You can find that out on the right-hand pages under the column "Untaxed Gains." Right now, Twentieth Century Growth's untaxed gain is small, only 7% of the portfolio. But a year ago, that figure was 22%.

In that same column, you'll also note many negative numbers. That means the fund has more unrealized losses than gains in the portfolio. That could be a tax shelter. The fund can't distribute losses to shareholders, but it can use them to offset future gains and avoid taxable distributions. Of course, buying a fund rife with losses means you're buying a loser—so you better be confident the fund can make a comeback.

Balancing all these analytics is not simple. But if you're a serious mutual fund investor, it's the only way to be sure that you and your fund are made for each other.

By Jeffrey M. Laderman in New York

Investment Styles: How They Fared

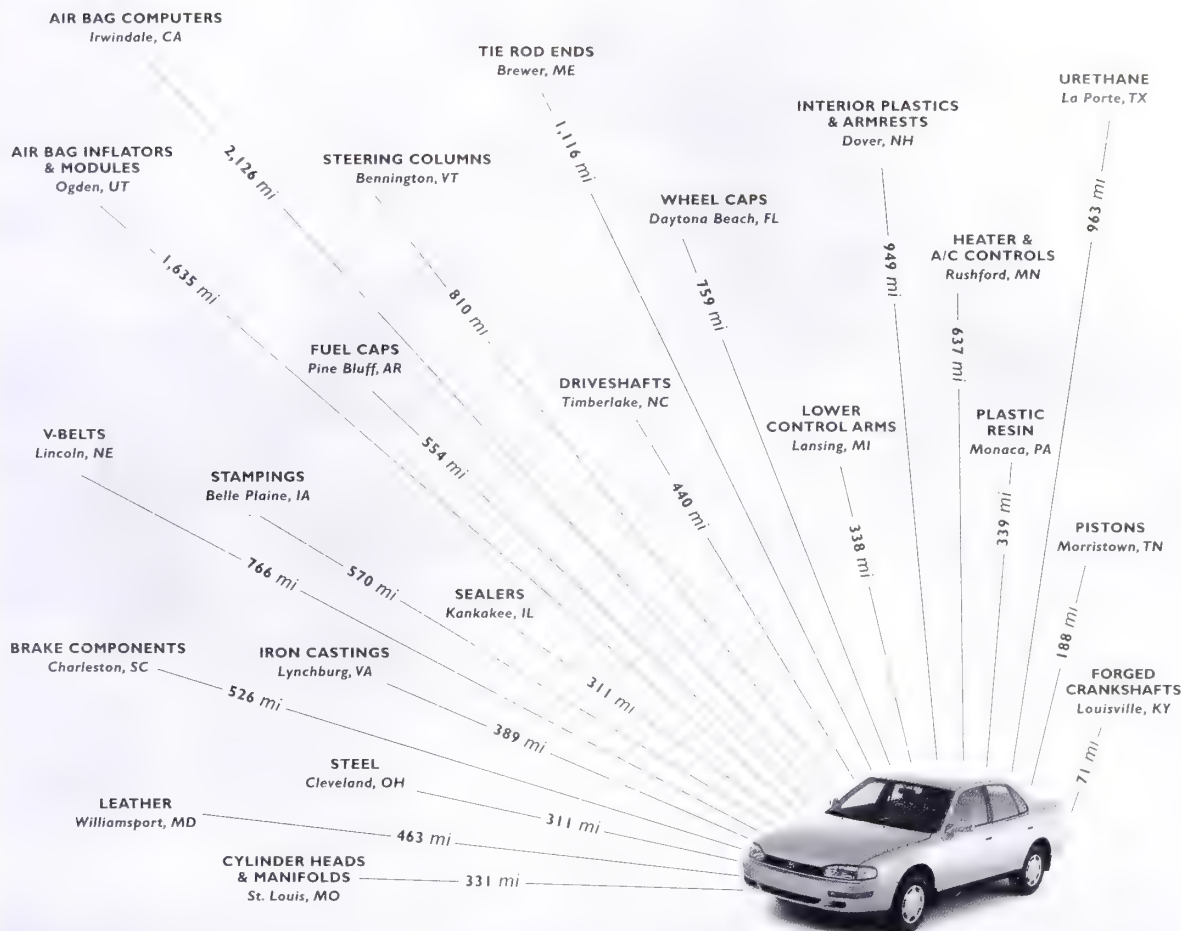
The Mutual Fund Scoreboard analyzes "investment style." First, we determine median market capitalization of a fund's stocks. Large-cap is more than \$5 billion; small, less than \$1 billion; and midcap, \$1 billion to \$5 billion. Then we measure the average price-earnings and price-book ratios to see if the stocks are "growth" or "value" and compare them with the stocks in the S&P 500. Those with p-e's and p-b's below those of the S&P index are deemed "value" funds; those higher, "growth" funds. Those that are close to the S&P averages are "blends."

		Investment Style		
		VALUE	BLEND	GROWTH
Median Market Capitalization	LARGE	LARGE-CAP VALUE -1.3%	LARGE-CAP BLEND -1.4%	LARGE-CAP GROWTH -1.0%
	MIDDLE	MID-CAP VALUE -2.8%	MID-CAP BLEND -1.5%	MID-CAP GROWTH -3.0%
	SMALL	SMALL-CAP VALUE -1.0%	SMALL-CAP BLEND -1.8%	SMALL-CAP GROWTH -1.3%

FUND AVERAGES ARE BASED ON 1994 PRETAX RETURNS

DATA: MORNINGSTAR INC.

Before you buy a Camry CHECK THE MILEAGE.



More than 270,000 Camrys are built every year in Georgetown, Kentucky.

EVERY YEAR, Toyota buys thousands of parts from communities right across the country. In fact, we buy more than \$4.6 billion per year in parts for both domestic and overseas production, from more than 440

U.S. suppliers. Whether it's engine blocks from Ohio, batteries from Tennessee or wiper systems from New York, our investment in local industries is paying off in the form of thousands of jobs across the United States.

INVESTING IN THE THINGS WE ALL CARE ABOUT. **TOYOTA**

For more information about Toyota in America with Toyota Motor Corporate Services, 9 West 57th Street, Suite 4900-J14, New York, NY 10019

Equity Funds

MUTUAL FUND SCOREBOARD

How To Use the Tables

BUSINESS WEEK RATING

Based on five-year risk-adjusted performance, relative to the S&P 500. Calculated by subtracting a fund's risk-of-loss factor (see RISK) from historical pretax total return. To get a positive rating, fund must beat the S&P 500 on a risk-adjusted basis. The ratings are as follows:

- ◆ ◆ ◆ SUPERIOR
- ◆ ◆ VERY GOOD

- ◆ GOOD
- ◆ AVG AVERAGE
- ◆ ◆ BELOW AVERAGE
- ◆ ◆ ◆ POOR
- ◆ ◆ ◆ ◆ VERY POOR

MANAGEMENT CHANGES

◆ indicates the fund's manager has held the job at least 10 years; ◆ indicates a new manager since Dec. 31, 1994.

S&P 500 COMPARISON

The pretax total returns for the S&P 500 are as follows: 1994, 1.3%; three-year average (1992-

1994), 6.3%; five-year average (1990-94), 8.7%; 10-year average (1985-94), 14.4%

SALES CHARGE

The cost of buying a fund, or the "load." Many load funds take the charge out of the initial investment, and for ratings purposes, performance is reduced by these charges. Loads may be levied on withdrawals, either as a flat fee or one that declines over time.

EXPENSE RATIO

Expenses for 1994 as a percentage of average net assets, a mea-

sure of how much shareholders pay for management. Footnotes indicate if a ratio includes 12(b)-1 plan, which spends holder money for marketing.

OBJECTIVE

Some funds specialize in a sector, which is indicated in this column. Other funds are growth funds, which follow: Asset allocation: Mix of stocks, bonds and cash, and possibly gold, real estate and securities. Balanced: Buy stocks and bonds. Equity-income: Emphasizes high-

FUND	RATING	OBJECTIVE	SIZE		FEES		1994 RETURNS (%)				RANK OBJECTIVE
			ASSETS \$MIL	% CHG 1993-4	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE- TAX	AFTER- TAX	YIELD		
AARP CAPITAL GROWTH	◆◆	Growth	649.0	0	No load	0.97	-10.0	-10.6	0.0	2283	
AARP GROWTH & INCOME	◆◆◆	Growth/income	2284.7	38	No load	0.76	3.1	1.1	2.9	163	
ABT UTILITY INCOME	◆◆	Utilities	99.9	-29	4.75	1.02†	-12.2	-13.5	5.1	23	
ACORN	◆◆	Small company	1982.8	-3	2.00*†	0.63	-7.6	-8.8	0.9	88	
ACORN INTERNATIONAL	◆◆	Foreign	1364.8	51	2.00*†	1.20	-3.8	-4.0	0.6	36	
ADVANTAGE GROWTH	◆	Growth	76.4	-5	4.00**	1.99†	-7.7	-8.1	0.5	2123	
ADVANTAGE INCOME	◆	Income	73.8	-9	4.00**	1.69†	-5.3	-7.0	4.8	17	
AFFILIATED	◆	Growth/income	4009.6	-2	5.75	0.63†	3.9	1.0	2.9	133	
AIM AGGRESSIVE GROWTH	◆◆◆	Maximum growth	714.7	161	5.50†	1.00†	17.2	17.2	0.0	33	
AIM CHARTER	◆	Growth/income	1475.1	-11	5.50	1.15†	-4.3	-6.0	2.4	1183	
AIM CONSTELLATION	◆◆	Maximum growth	3703.5	27	5.50	1.20†	1.3	0.5	0.0	33	
AIM GROWTH A	◆◆◆	Growth	123.7	-16	5.50	1.13†	-5.0	-6.0	0.0	1863	
AIM INTERNATIONAL EQUITY A	◆◆	Foreign	653.4	36	5.50	1.63†	-3.3	-4.4	0.3	36	
AIM SUMMIT	◆	Growth	746.4	5	8.50	0.72	-2.8	-4.2	1.1	1543	
AIM UTILITIES A	◆◆	Utilities	150.0	-25	5.50	1.16†	-11.6	-13.0	5.3	23	
AIM VALUE A	◆◆	Growth	1358.3	78	5.50	1.01†	3.3	2.8	0.7	363	
AIM WEINGARTEN	◆	Growth	3667.6	-22	5.50	1.20†	-0.3	-3.4	0.4	1003	
ALGER GROWTH	◆	Growth	71.4	74	5.00**	2.34†	-1.6	-2.2	0.0	1323	
ALGER SMALL CAPITALIZATION	◆	Small company	294.3	2	5.00**	2.17†	-4.6	-4.6	0.0	68	
ALLIANCE A	◆	Growth	732.2	-12	4.25	1.04†	-2.5	-6.7	0.2	1473	
ALLIANCE BALANCED SHARES A	◆	Balanced	143.8	-16	4.25	1.27†	-5.8	-6.7	3.0	45	
ALLIANCE GROWTH & INCOME A	◆	Growth/income	387.8	-13	4.25	1.04†	-4.2	-6.3	2.3	1143	
ALLIANCE GROWTH B	◆◆	Growth	812.2	380	4.00**	2.10†	-1.8	-2.4	0.0	1373	
ALLIANCE INTERNATIONAL A	◆◆◆	Foreign	176.8	-2	4.25	1.82†	5.7	3.0	0.0	68	
ALLIANCE NEW EUROPE A	◆	Europe	78.6	-14	4.25	2.30†	4.6	4.4	0.7	71	
ALLIANCE PREMIER GROWTH B	◆	Growth	137.0	-12	4.00**	2.70†	-6.2	-7.8	0.0	1933	
ALLIANCE QUASAR A	◆◆◆	Maximum growth	129.8	-34	4.25	1.63†	-7.3	-11.8	0.0	23	
ALLIANCE TECHNOLOGY A	◆◆◆	Technology	215.7	24	4.25	1.66†	28.5	25.1	0.0	71	
AMCAP	◆	Growth	2877.2	-7	5.75	0.72†	-0.2	-2.7	1.0	983	
AMCORE VINTAGE EQUITY	◆	Growth	139.1	23	No load	0.54†	2.0	1.5	1.5	513	
AMERICA'S UTILITY	◆	Utilities	123.6	-5	No load	1.21	-13.1	-14.4	4.9	30	
AMERICAN BALANCED	◆	Balanced	2081.9	22	5.75	0.71†	0.3	-1.2	4.6	15	
AMERICAN CAPITAL COMSTOCK A	◆	Growth/income	871.8	-11	5.75	0.98†	-3.7	-9.6	2.1	1103	
AMERICAN CAPITAL EMERGING GROWTH A	◆	Small company	677.6	16	5.75	1.18†	-7.1	-7.8	0.0	78	
AMERICAN CAPITAL ENTERPRISE A	◆	Growth	749.3	-5	5.75	1.03†	-0.2	-1.9	0.7	973	
AMERICAN CAPITAL EQUITY-INCOME B	◆	Equity-income	241.8	110	5.00**	1.81†	-2.7	-4.0	2.8	20	
AMERICAN CAPITAL GROWTH & INC. A	◆	Growth/income	205.4	-3	5.75	1.12†	-1.7	-4.9	2.3	903	
AMERICAN CAPITAL PACE A	◆	Growth	2060.7	-16	5.75	1.02†	-3.7	-7.1	1.1	1703	
AMERICAN CAPITAL RESOURCES	◆◆	Natural resources	176.2	-23	No load	0.84	-9.7	-10.9	4.3	11	
AMERICAN GROWTH	◆	Growth	69.8	2	5.75	1.34	-4.0	-9.1	1.4	1783	
AMERICAN LEADERS A	◆	Growth/income	239.8	7	6.00*	1.18†	0.0	-1.1	1.6	623	
AMERICAN NATIONAL	◆	Growth/income	5278.6	2	5.75	0.59†	0.3	-2.0	4.0	563	
AMERICAN NATIONAL GROWTH	◆	Growth	113.3	0	5.75	0.98	4.4	0.8	1.4	233	
AMERICAN NATIONAL INCOME	◆	Equity-income	114.2	-5	5.75	1.10	-1.1	-4.5	2.4	133	
AMERICAN PERFORMANCE EQUITY	◆	Growth	72.1	33	4.00	1.12†	-1.2	-4.9	1.7	1203	

Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts. § Holding is less than 0.5% of assets.

income: Maximizes current income with stocks and bonds. Growth/income: Strives for capital appreciation with some growth. Maximum income: Makes greater risks, and uses options, margin, or short sales.

TOTAL RETURN

Net gain to investors, reinvestment of dividends, capital gains at end prices.

TOTAL RETURN

Return adjusted for federal income taxes on ordinary income and capital gains taxed at highest rate in each year; uses average income since capital gains are assumed long-term.

Distributions as a percent

of net asset value, adjusted for capital gains distributions.

RANK WITHIN OBJECTIVE

1994 performance ranking relative to other funds with same objective.

TREND

A fund's relative performance during the four 30-month periods from Jan. 1, 1985 to Dec. 31, 1994. Boxes read from left to right, and the level of green indicates performance relative to all other funds in that period: ■ for the top quartile; ■ for the second quartile; ■ for the third quartile; ■ for the bottom quartile. An empty box indicates no data for that period.

TURNOVER

Trading activity, the lesser of purchases or sales divided by average monthly assets.

% CASH

Portion of fund assets not invest-

ed in stocks or bonds. A negative number means the fund has borrowed to buy securities.

PRICE-EARNING RATIO

The average, weighted price-earnings ratio of stocks in a fund's portfolio, based on last 12 month's earnings.

STYLE

Each fund has a two-letter designation describing the characteristics of the fund's portfolio. L, M, or S, stands for large-, medium-, and small-capitalization stocks. V stands for value, an investment style that emphasizes stocks with lower-than-average p-e's and price-to-book value ratios. G indicates growth stocks, which have higher p-e's and p-b's. B is a blend of the two.

UNTAXED GAINS

Percentage of assets in portfolio that are unrealized and undistrib-

uted capital gains. A negative figure indicates losses that may offset future gains.

LARGEST HOLDING

Comes from the latest available fund reports.

RISK

Potential for losing money in a fund, or risk-of-loss factor. For each fund, the three-month Treasury bill return is subtracted from the monthly total return for each of the 60 months in the ratings period. When a fund has not performed as well as Treasury bills, the monthly result is negative. The sum of these negative numbers is divided by the number of months. The result is a negative number, and the greater its magnitude, the higher the risk of loss. This number is the basis for BW ratings and the RISK column.

ANNUAL TOTAL RETURNS (%)				TREND	PORTFOLIO DATA							RISK	TELEPHONE	
5 YEARS	10 YEARS				TURNOVER	% CASH	P-E	STYLE	UNTAXED	LARGEST HOLDING			TOLL-FREE	IN-STATE
PRETAX	PRETAX	RETAX	RETAX	BW 10-YEAR ANALYSIS			RATIO		GAINS (%)	COMPANY (% ASSETS)			(800)	
5.3	3.6	12.0	10.4		Average	5	24	MG	-1	Tele-Communications CI A(5)	High	322-2282	MA	617-330-5400
10.0	8.4	13.5	11.7		Low	8	22	MB	6	Xerox(2)	Low	322-2282	MA	617-330-5400
3.1	0.7	9.8	6.4		Low	2	15	LV	-8	Sprint(5)	Low	553-7838	FL	407-655-7255
13.1	11.4	16.6	14.0		Low	9	27	SG	34	Liberty Media CI A(4)	Average	922-6769		
					Low	14	24	SG	5	Security Patrols(1)		922-6769		
7.6	6.2				Average	1	19	LB	9	First Financial Management(4)	Average	241-2039	CT	203-241-2030
7.3	5.5				Average	12	15	MV	1	Dow Chemical(2)	Very low	241-2039	CT	203-241-2030
8.9	6.0	13.1	9.4		Average	4	17	LV	13	Minnesota Mining & Mfg(3)	Low	874-3733	NY	212-848-1800
23.5	21.7	16.0	14.6		Average	7	21	SB	18	DSC Communications(1)	High	347-1919	TX	713-626-1919
9.6	8.1	14.0	11.0		High	7	18	LB	0	FNMA(2)	Low	347-1919	TX	713-626-1919
17.4	17.2	19.8	16.7		Average	16	22	MG	17	Compaq Computer(1)	High	347-1919	TX	713-626-1919
5.1	2.1	10.5	7.0		Very high	10	20	MB	6	Texas Instruments(2)	High	347-1919	TX	713-626-1919
9.8	7.8	13.3	11.2		Average	8	27	MB	6	Mannesmann (Germany)(1)		347-1919	TX	713-626-1919
5.2	2.7				High	5	17	MB	7	General Electric(2)	Average	347-1919	TX	713-626-1919
					Average	5	14	MV	-14	Southwestern Bell(3)	Average	347-1919	TX	713-626-1919
15.8	13.5	16.6	13.7		Very high	10	16	MV	5	Texas Instruments(4)	Average	347-1919	TX	713-626-1919
9.1	8.0	15.9	14.0		High	9	17	LB	8	Texas Instruments(2)	Average	347-1919	TX	713-626-1919
14.0	12.2				High	5	22	MB	7	Cracker Barrel Old Country(3)	High	992-3863	NY	201-547-8320
13.0	11.9				High	7	28	SG	14	Altera(3)	Very high	992-3863	NY	201-547-8320
10.3	6.0	13.8	8.9		Average	3	19	LB	8	Intel(7)	High	227-4618	NJ	201-319-4000
5.4	4.3	10.7	7.8		Very high	0	16	LB	-1	General Electric(3)	Low	227-4618	NJ	201-319-4000
6.6	3.4	12.5	7.8		High	4	17	LB	1	Royal Dutch Petroleum (ADR)(3)	Average	227-4618	NJ	201-319-4000
15.8	13.1				Average	10	18	MB	-1	General Motors(5)	Average	227-4618	NJ	201-319-4000
1.6	0.5	15.8	12.7		High	4	38	LB	9	Nomura Securities(3)	High	227-4618	NJ	201-319-4000
					High	2	21	LV	-6	Amev(3)		227-4618	NJ	201-319-4000
2.6	1.1	11.5	9.1		Average	2	18	LG	-3	United Healthcare(6)		227-4618	NJ	201-319-4000
22.0	17.8	17.1	14.1		High	8	19	SB	9	Consolidated Stores(3)	Very high	227-4618	NJ	201-319-4000
9.3	6.8	13.0	10.2		Average	7	25	MG	38	Microsoft(6)	Very high	227-4618	NJ	201-319-4000
					Low	19	21	LG	24	Time Warner(4)	Average	421-4120	CA	213-486-9200
					Very low	0	18	LB	3	American Cyanamid(2)		438-6375		
8.5	6.2	12.4	9.1		Very low	15	15	MV	-15	Public Service Colorado(4)		487-3863	VA	804-649-1315
7.4	4.2	11.3	7.8		Low	22	17	LV	2	American Home Products(2)	Very low	421-4120	CA	415-421-9360
15.6	14.0	13.0	11.0		Average	2	18	LB	-3	Philip Morris(3)	Average	421-5666	TX	713-993-0500
10.2	7.3	13.1	9.4		Average	12	24	MG	12	Tellabs(2)	High	421-5666	TX	713-993-0500
					Very high	3	20	MG	7	Philip Morris(3)	Average	421-5666	TX	713-993-0500
9.1	6.6	10.9	7.8		High	5	17	LB	0	IBM(1)		421-5666	TX	713-993-0500
6.7	3.5	10.6	7.5		High	7	18	LB	2	IBM(2)	Average	421-5666	TX	713-993-0500
1.6	0.1				High	4	20	LB	0	Philip Morris(2)	Average	421-5666	TX	713-993-0500
9.2	6.2	10.5	7.3		Very low	1	13	MV	-7	Panhandle Eastern(5)	Average	343-3355	MD	301-657-1500
					Average	59	14	LV	-5	Mylan Laboratories(4)	Average	525-2406	CO	303-623-6137
10.0	8.0	11.9	9.1		Low	6	16	LB	15	Raytheon(3)	Average	245-5051	PA	412-288-1900
8.2	5.7	13.0	9.9		Low	13	16	LV	15	DuPont(3)	Low	421-4120	CA	213-486-9200
7.7	4.9	12.1	8.7		Average	5	18	LB	3	Johnson & Johnson(3)	Average	231-4639	TX	409-763-8772
8.0	5.3	11.5	8.2		Average	8	17	LB	0	Texaco(3)	Low	231-4639	TX	409-763-8772
					High	2	17	LB	-2	Procter & Gamble(2)		762-7085		

DATA: MORNINGSTAR INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1994 RETURNS (%)				RANKING OBJ. T
			ASSETS \$MIL	% CHG 1993-4	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE- TAX	AFTER- TAX	YIELD		
AMSOUTH BALANCED		Balanced	239.4	22	4.50	0.84	-0.4	-2.3	3.8	15	
AMSOUTH EQUITY	AVG	Growth	207.9	24	4.50	0.94	0.4	-1.1	2.1	793	
ARIEL APPRECIATION A (a)	AVG	Growth	128.5	-41	No load	1.35†	-8.4	-10.2	0.3	2203	
ARIEL GROWTH (b)	♦♦	Small company	130.8	-42	No load†	1.25†	-4.2	-6.0	0.8	18	
ATLAS GROWTH & INCOME A		Growth/income	68.7	22	3.00	1.04†	-1.2	-1.9	1.2	853	
BABSON ENTERPRISE	♦♦	Small company	190.5	-3	No load†	1.09	2.4	-0.5	0.2	28	
BABSON GROWTH	♦	Growth	226.5	-8	No load	0.86	-0.6	-2.8	1.6	1063	
BABSON VALUE	♦	Growth/income	122.0	167	No load	1.00	2.5	1.2	1.9	223	
BAILARD BIEHL & KAISER INTL. EQTY.	♦♦♦	World	148.8	-32	No load	1.39	-12.6	-12.6	0.0	40	
BARON ASSET	AVG	Small company	84.3	38	No load	1.60†	7.4	6.5	0.0	18	
BARTLETT BASIC VALUE	AVG	Growth/income	93.2	-7	No load	1.22	0.4	-2.0	1.6	553	
BENHAM EQUITY GROWTH		Growth	97.6	1	No load	0.75	-0.2	-1.6	2.5	962	
BENHAM GOLD EQUITIES INDEX	♦♦♦	Precious metals	570.6	-8	No load	0.60	-16.7	-16.9	0.2	11	
BENHAM INCOME & GROWTH		Growth/income	224.8	-2	No load	0.75	-0.5	-2.7	3.0	743	
BENHAM UTILITIES INCOME		Utilities	152.3	-21	No load	0.75	-10.0	-11.4	5.0	23	
BERGER 100	♦♦	Growth	2113.0	28	No load	1.70†	-6.7	-6.7	0.0	2003	
BERGER 101	♦	Growth/income	368.3	95	No load	1.81†	-9.1	-9.4	1.2	1363	
BERGER SMALL COMPANY GROWTH		Small company	291.2	NM	No load	2.05†	13.7	13.7	0.1	3	
BERNSTEIN INTERNATIONAL VALUE		Foreign	1392.8	126	No load	1.39	3.8	2.5	0.7	10	
BILTMORE BALANCED		Balanced	194.7	16	4.50	0.79	-0.5	-2.0	3.5	15	
BILTMORE EQUITY		Growth/income	86.9	41	4.50	0.89	2.0	0.8	2.0	273	
BILTMORE EQUITY INDEX		Growth/income	183.7	23	4.50	0.49	0.9	0.0	2.5	473	
BLANCHARD GLOBAL GROWTH	♦	Asset allocation	93.8	-2	No load	2.61†	-7.5	-8.2	2.0	33	
BLANCHARD PRECIOUS METALS	♦♦♦	Precious metals	77.3	7	No load	2.46†	-15.0	-18.4	0.0	11	
BNY HAMILTON EQUITY-INCOME		Equity-income	135.1	20	3.00	1.03	-2.6	-3.4	2.9	23	
BRANDYWINE	♦♦	Growth	2299.3	51	No load	1.10	0.0	-1.6	0.0	943	
BT INVESTMENT EQUITY 500 INDEX		Growth	192.1	NM	No load	0.25	1.1	0.2	2.1	663	
BURNHAM A	AVG	Growth/income	102.3	-14	3.00	1.50†	-1.8	-4.0	4.3	913	
CALVERT SOCIAL INVMT. EQUITY A	♦♦♦	Growth	90.3	4	4.75	1.16†	-12.2	-13.9	0.2	2333	
CALVERT SOCIAL INVMT. MANAGED A	AVG	Balanced	489.7	-10	4.75	1.23†	-4.7	-5.9	3.3	45	
CALVERT WORLD VALUES GLOB. EQTY. A		World	176.6	119	4.75	2.10†	-2.7	-4.2	4.2	24	
CAPITAL EXCHANGE	♦	Growth/income	89.6	61	4.00	0.78	6.0	5.5	1.5	43	
CAPITAL INCOME BUILDER	♦♦	Equity-income	3596.5	18	5.75	0.72†	-2.3	-3.9	5.2	23	
CAPITAL MARKET INDEX		Growth/income	161.6	2	No load	0.13	1.0	0.3	2.5	443	
CAPITAL WORLD GROWTH & INCOME		World	2827.1	60	5.75	NA †	1.2	-0.1	2.9	14	
CAPSTONE GROWTH (c)	♦♦	Growth	75.9	-26	4.75	1.24†	-7.8	-8.4	0.8	2143	
CARDINAL	♦	Growth/income	229.4	-16	6.00	0.72	-3.2	-5.9	2.9	1063	
CENTURY SHARES	♦	Financial	206.1	-12	No load	1.02	-3.9	-5.5	2.0	30	
CGM CAPITAL DEVELOPMENT	♦♦	Growth	401.7	-23	No load†	0.84	-22.9	-23.7	0.3	2383	
CGM MUTUAL	♦	Balanced	1063.4	12	No load	0.93	-9.7	-10.9	4.2	55	
CHESAPEAKE GROWTH		Growth	235.3	246	3.00	1.54	7.0	7.0	0.0	163	
CLIPPER	AVG	Growth	245.7	-14	No load	1.13	-2.5	-4.1	1.5	1463	
COHEN & STEERS REALTY SHARES		Specialty	458.5	194	No load	1.10	8.3	6.7	5.0	20	
COLONIAL A	AVG	Growth/income	537.0	4	5.75	1.14†	-2.1	-4.5	2.3	953	
COLONIAL GROWTH SHARES A	♦♦	Growth	151.4	-9	5.75	1.22†	-2.7	-5.4	0.8	1523	
COLONIAL INTL. FUND FOR GROWTH B		Foreign	99.2	NM	5.00**	2.50†	-8.4	-8.4	0.0	50	
COLONIAL U.S. FUND FOR GROWTH B		Growth	163.3	30	5.00**	2.24†	-1.0	-2.9	0.4	1143	
COLONIAL UTILITIES B		Utilities	743.9	-23	5.00**	1.98†	-11.0	-12.3	5.0	20	
COLUMBIA BALANCED		Balanced	249.7	34	No load	0.72	0.1	-1.0	3.7	5	
COLUMBIA COMMON STOCK		Growth/income	124.3	23	No load	0.84	2.1	1.2	1.6	263	
COLUMBIA GROWTH	AVG	Growth	591.7	-2	No load	0.83	-0.6	-2.1	1.0	1053	
COLUMBIA INTERNATIONAL STOCK		Foreign	118.5	64	No load	1.71	-2.5	-2.9	0.0	30	
COLUMBIA SPECIAL	AVG	Small company	889.5	15	No load	1.11	2.3	0.4	0.4	20	
COMMON SENSE GROWTH	♦	Growth	1951.7	-1	8.50	1.12	-2.3	-4.5	1.1	1433	
COMMON SENSE GROWTH & INCOME	♦	Growth/income	609.3	-9	8.50	1.02	-3.2	-6.6	2.0	1053	
COMPASS CAPITAL EQUITY-INCOME	♦	Equity-income	279.0	5	3.75	0.92	0.6	-2.4	2.4	10	
COMPASS CAPITAL GROWTH	♦♦	Growth	131.0	-14	3.75	0.95	0.1	-0.7	0.5	903	
COMPOSITE BOND & STOCK A	♦	Balanced	183.4	-3	4.50	1.14†	-2.1	-3.6	4.2	25	
COMPOSITE GROWTH A	AVG	Growth/income	100.0	4	4.50	1.17†	2.6	1.1	1.6	203	
COMPOSITE NORTHWEST 50 A	♦♦	Growth	146.9	-12	4.50	1.09†	-1.4	-1.6	0.5	1253	
COMSTOCK PARTNERS STRATEGY O	♦	Asset allocation	403.3	-22	4.50†	1.07†	-3.5	-5.4	6.5	20	
CONNECTICUT MUTUAL GROWTH	♦	Growth	78.4	22	5.00	0.96	-0.3	-2.0	1.8	953	
CONNECTICUT MUTUAL TOTAL RETURN	♦♦	Asset allocation	177.9	4	5.00	0.92	-2.1	-3.8	4.0	13	
COPLEY	♦	Growth/income	73.5	-9	No load	1.10	-7.7	-7.7	0.0	1313	
CORABBE HUSON ASSET ALLOCATION	♦♦	Asset allocation	107.1	16	No load	1.47†	-0.8	-2.6	2.5	10	
CORABBE HUSON EQUITY	♦♦♦	Growth	155.5	277	No load	1.49†	1.6	0.9	0.9	563	
CORABBE HUSON SPECIAL	♦♦♦	Growth	377.5	1201	No load	1.48†	11.7	10.6	0.3	70	
DEAN WITTER AMERICAN VALUE	♦	Growth	1490.1	22	5.00**	1.71†	-6.7	-7.1	0.0	1953	
DEAN WITTER CAPITAL GROWTH		Growth	439.5	-33	5.00**	1.90†	-3.0	-3.0	0.0	1573	
DEAN WITTER DEVELOPING GROWTH	♦♦	Small company	338.1	18	5.00**	1.77†	-4.6	-4.8	0.0	60	

* Includes redemptions fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts. § Holding is less than 0.5% of assets.
(a) Formerly Calvert World Appreciation A. (b) Formerly Calvert-Ariel Growth. (c) Formerly Capstone U.S. Trend.

ANNUAL TOTAL RETURNS (%)				TREND	PORTFOLIO DATA				RISK		TELEPHONE	
5 YEARS PRETAX AFTERTAX	10 YEARS PRETAX AFTERTAX	BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)			TOLL-FREE (800)	IN-STATE
7.9	6.3		Very low	8	18	LV	1	Ford Motor(2)			451-8379	OH 205-581-7530
8.0	7.3		Very low	9	18	LV	4	Ford Motor(3)	Average		451-8379	OH 205-581-7530
5.3	3.7		Very low	6	15	SV	10	Interco(4)	Average		292-7435	IL 301-951-4820
			Very low	-1	16	SV	20	Longs Drug Stores(5)	Average		292-7435	IL 301-951-4820
			Very high	-2	18	MB	3	Geon(2)			933-2852	
12.3	9.7		Low	5	19	SV	14	Anthony Industries(2)	Average		422-2766	MO 816-471-5200
6.4	4.7		Very low	3	16	LV	33	Computer Sciences(3)	Average		422-2766	MO 816-471-5200
10.7	9.2		Low	5	19	MV	6	Safety-Kleen(3)	Average		422-2766	MO 816-471-5200
-2.6	-3.0		Very high	14	26	MB	6	Nichiei(2)	High		882-8383	CA 415-571-5800
10.5	9.9		Average	0	29	SG	25	Robert Half International(9)	High		992-2766	NY 212-759-7700
7.1	5.6		Low	7	16	MV	12	Potash of Saskatchewan(3)	Average		800-4612	OH 513-621-4612
-0.3	-0.4		High	1	15	LB	2	AT&T(4)			331-8331	CA 415-965-4274
			Low	0	35	MG	5	American Barrick Resources(25)	Very high		331-8331	CA 415-965-4274
			Low	2	15	LB	2	General Electric(4)			331-8331	CA 415-965-4274
rated				1	14	LV	-19	Southwestern Bell(4)			331-8331	CA 415-965-4274
16.9	16.3		Average	9	26	MG	10	Oracle Systems(2)	High		333-1001	CO 303-329-0200
11.8	10.9		Low	11	18	MB	-4	Nokia (ADR)(2)	Average		333-1001	CO 303-329-0200
				16	34	SG	7	Level One Communications(1)			333-1001	
rated			Low	3	29	MV	3	Fuji Photo Film(3)				NY 212-756-4097
rated				8	17	LV	-3	FNMA(1)			462-7538	
rated				11	18	LB	0	Royal Dutch Petroleum(3)			462-7538	
rated				0	18	LB	2	Exxon(3)			462-7538	
4.4	2.6		High	24	23	MB	-4	Citizens First Bancorp (NJ)(1)	Low		922-7771	NY 212-779-7979
0.9	0.1		High	10	32	MG	-14	Placer Dome(11)	Very high		922-7771	NY 212-779-7979
rated			Average	13	21	LB	-1	Royal Dutch Petroleum(2)			426-9363	
16.3	13.8		Very high	31	24	MG	7	LSI Logic(3)	High		656-3017	DE 302-656-6200
rated			Low	5	18	LB	-1	General Electric(3)			943-2222	
6.0	3.2		Average	7	21	LB	5	Contel Cellular CI A(3)	Very low		874-3863	NY 212-262-3100
2.4	1.7		Low	0	19	MB	-6	Toys 'R' Us(3)	Average		368-2748	MD 301-951-4820
5.4	3.8		Low	7	18	MB	6	May Department Stores(2)	Very low		368-2748	MD 301-951-4820
rated			Low	6	26	MB	-2	Malayan Banking(3)			368-2748	MD 301-951-4820
10.6	10.0		Very low	1	18	LB		Albertson's(7)	Low		225-6265	
10.1	8.3		Very low	14	15	LV	2	American Home Products(2)	Very low		421-4120	CA 213-486-9200
rated				NA	NA			NA			328-7408	
rated				13	16	LV	4	Intl Nederlander Groep(2)			421-4120	CA 213-486-9200
5.2	3.3		Average	2	18	LB	18	General Electric(5)	Average		262-6631	TX 713-750-8000
6.9	4.9		Low	8	16	LV	17	Philip Morris(4)	Low		848-7734	OH 614-464-6852
8.1	6.3		Low	1	12	MV	51	General RE(6)	High		321-1928	MA 617-482-3060
18.7	14.3		High	0	17	SG	-7	Stone Container(8)	Very high		345-4048	MA 617-859-7714
10.7	8.2		High	1	13	LV	-2	Chemical Banking(5)	Average		345-4048	MA 617-859-7714
rated				11	22	SB	4	KLA Instruments(4)			525-3863	
9.0	6.8		Average	2	13	LV	5	FNMA(9)	Average		776-5033	CA 310-247-3940
			Average	10	25	SB	1	Kimco Realty(5)			437-9912	NY 212-832-3232
8.1	6.1		Average	3	13	MV	7	Nynex(2)	Low		248-2828	MA 617-426-3750
7.3	5.1		High	3	14	MV	3	FNMA(4)	Average		248-2828	MA 617-426-3750
rated			Very low	2	NA			NA			248-2828	MA 617-426-3750
rated			High	1	16	LB	3	Exxon(3)			248-2828	MA 617-426-3750
rated			Low	1	14	MV	-23	Nynex(3)			248-2828	MA 617-426-3750
			High	7	20	LB	1	FNMA(2)			547-1707	OR 503-222-3606
			Average	13	20	LG	7	FNMA(3)			547-1707	OR 503-222-3606
10.3	7.7		High	7	20	MB	6	Philip Morris(3)	Average		547-1707	OR 503-222-3606
13.3	11.3		High	15	38	LB	4	Mitsubishi Heavy Industries(2)			547-1707	OR 503-222-3606
8.9	6.8		High	15	24	MB	6	US Bancorp (OR)(1)	High		547-1707	OR 503-222-3606
7.6	5.7		High	3	20	LB	2	IBM(2)	Average		544-5445	
			Average	7	17	LB	4	IBM(2)	Average		544-5445	
10.1	7.7		High	2	18	MV	-2	Alcoa(5)	Low		451-8371	
6.2	4.5		High	5	20	MB	2	Amoco(2)	Average		451-8371	
7.4	5.6		Low	0	16	LV	1	Hanson (ADR)(2)	Very low		543-8072	WA 509-353-3400
7.8	6.0		Average	3	18	LV	11	Microsoft(3)	Low		543-8072	WA 509-353-3400
8.5	8.0		Very low	1	21	MB	17	Microsoft(8)	High		543-8072	WA 509-353-3400
6.1	3.2		Low	14	32	MG	6	Placer Dome(2)	Very low		645-6561	NY 718-895-1206
11.2	8.5		High	10	15	MV	7	Compaq Computer(2)	Average		234-5606	
9.8	7.2		High	7	15	MV	0	Safeway(1)	Very low		234-5606	
6.7	6.7		Average	27	15	MV	8	Texas Utilities(3)	Very low		424-8570	DC 508-674-8459
9.6	7.8		High	10	17	MB	2	IBM(1)	Very low		541-9732	OR 503-295-0919
14.7	13.1		High	20	16	MV	2	IBM(2)	Low		541-9732	OR 503-295-0919
19.5	16.0		Average	18	24	SB	3	Cray Research(4)	High		541-9732	OR 503-295-0919
12.2	10.9		Very high	22	22	LG	-1	Microsoft(2)	Average		869-3863	NY 212-392-2550
			Low	5	18	MB	-3	Tootsie Roll Industries(3)			869-3863	NY 212-392-2550
11.6	11.2		Very high	3	24	SG	12	Danka Business Systems (ADR)(2)	Very high		869-3863	NY 212-392-2550

DATA: MORNINGSTAR INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1994 RETURNS (%)				RANK OF 100
			ASSETS \$MIL	% CHG 1993-4	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE- TAX	AFTER- TAX	YIELD		
DEAN WITTER DIVERSIFIED INCOME		Income	412.7	108	5.00**	1.54†	-1.3	-3.6	7.8	71	
DEAN WITTER DIVIDEND GROWTH 📈	AVG	Growth/income	6696.0	2	5.00**	1.41†	-3.2	-3.8	2.3	104	
DEAN WITTER EUROPEAN GROWTH		Europe	726.3	40	5.00**	2.24†	6.9	4.4	0.0	71	
DEAN WITTER GLOBAL DIV. GRTH. SECS.		World	1733.8	96	5.00**	2.03†	7.1	6.0	1.1	74	
DEAN WITTER HEALTH SCIENCES		Health care	243.1	-14	5.00**	2.30†	-6.5	-6.5	0.0	71	
DEAN WITTER MANAGED ASSETS	👑👑	Asset allocation	408.7	61	5.00**	1.79†	2.7	0.5	2.3	71	
DEAN WITTER NAT. RESOURCE DEV. SEC.	👑👑	Natural resources	136.5	4	5.00**	1.99†	-0.9	-3.2	0.7	71	
DEAN WITTER PACIFIC GROWTH		Pacific	1417.7	31	5.00**	2.20†	-17.5	-18.7	0.0	71	
DEAN WITTER PREC. METALS & MINS.		Precious metals	66.7	13	5.00**	2.33†	-11.5	-12.1	0.0	71	
DEAN WITTER STRATEGIST	👑	Asset allocation	766.0	-7	5.00**	1.62†	-1.9	-3.5	2.1	71	
DEAN WITTER UTILITIES	AVG	Utilities	2828.6	-27	5.00**	1.59†	-9.3	-10.7	5.0	71	
DEAN WITTER VALUE-ADDED MKT. EQTY.	👑	Growth/income	495.2	44	5.00**	1.68†	0.1	-0.3	0.5	63	
DEAN WITTER WORLDWIDE INVMNT 📈	👑👑	World	575.7	61	5.00**	2.40†	-7.1	-8.1	0.1	71	
DELAWARE A	AVG	Balanced	439.4	-12	5.75	0.94†	-1.4	-2.8	3.6	71	
DELAWARE DECATUR INCOME A (d)	👑	Equity-income	1150.7	-24	5.75	0.74†	-0.8	-2.8	4.4	71	
DELAWARE DECATUR TOTAL RET. A (e)	👑	Growth/income	403.0	-7	5.75	1.22†	-0.5	-2.4	3.2	71	
DELAWARE DELCAP A	👑👑	Growth	761.8	-24	5.75	1.35†	-5.3	-7.3	0.0	189	
DELAWARE TREND A 📈	👑	Maximum growth	268.6	-3	5.75	1.37†	-10.0	-11.6	0.0	71	
DELAWARE VALUE A	AVG	Growth	180.3	19	5.75	1.44†	-7.0	-7.6	0.8	203	
DG EQUITY		Growth	233.3	-18	2.00	0.96†	1.8	0.9	1.5	53	
DODGE & COX BALANCED 📈	👑👑	Balanced	708.4	51	No load	0.58	2.1	0.6	3.9	71	
DODGE & COX STOCK 📈	👑	Growth/income	524.4	23	No load	0.61	5.2	4.0	2.1	71	
DREYFUS	👑	Growth/income	2466.3	-14	No load	0.74	-4.3	-5.6	1.7	113	
DREYFUS APPRECIATION	AVG	Growth	228.5	-4	No load	1.07†	3.6	3.0	1.8	293	
DREYFUS BALANCED		Balanced	89.0	56	No load	0.69†	4.0	2.6	3.4	71	
DREYFUS CAP. GROWTH (PREMIER) 📈	AVG	Growth	555.8	-9	3.00	1.12	-7.0	-8.2	3.0	203	
DREYFUS CAP. VALUE A (PREMIER)	👑👑	Asset allocation	377.4	-11	4.50	1.23	-3.9	-4.6	2.3	71	
DREYFUS CORE VALUE INV. (f)	👑👑	Growth	319.1	-7	No load	1.11†	0.3	-3.2	1.5	825	
DREYFUS EDISON ELECTRIC INDEX		Utilities	71.7	-33	No load	0.75	-12.7	-14.4	6.4	71	
DREYFUS GLOBAL GROWTH (g)	AVG	World	137.3	-6	3.00	1.50†	-7.3	-7.3	0.0	71	
DREYFUS GLOBAL INV. A (PREMIER)		World	75.3	3	4.50	1.66†	-5.5	-6.2	1.0	71	
DREYFUS GROWTH & INCOME		Growth/income	1640.8	37	No load	1.24	-5.2	-6.1	2.3	123	
DREYFUS GROWTH OPPORTUNITY 📈	👑👑	Growth	366.7	-25	No load	1.09	-6.3	-11.5	0.9	199	
DREYFUS INTL. EQUITY		Foreign	167.8	74	No load	NA †	-5.4	-5.9	0.2	71	
DREYFUS NEW LEADERS	👑	Small company	388.0	22	1.00*	1.22†	-0.1	-2.4	0.2	71	
DREYFUS SPECIAL GROWTH INV. (h)	👑👑	Growth	68.3	-15	No load	1.54†	-18.3	-18.3	0.0	233	
DREYFUS STRATEGIC GROWTH	👑	Maximum growth	103.4	137	3.00	1.59†	2.7	3.1	0.0	71	
DREYFUS STRATEGIC INVESTING A	👑	Growth	227.9	-13	4.50	1.74†	-11.4	-12.1	0.3	233	
DREYFUS THIRD CENTURY 📈	👑	Growth	349.0	-32	No load	1.17†	-7.5	-11.1	0.9	208	
EBI EQUITY	AVG	Growth/income	77.9	-11	No load	2.25†	2.7	0.1	0.6	13	
EBI FLEX	👑👑	Asset allocation	243.8	-12	No load	2.25†	0.6	-1.5	2.4	71	
EBI MUTIFLEX		Asset allocation	120.3	943	No load	2.50†	-1.0	-1.5	1.6	71	
ECLIPSE FINANCIAL ASSET EQUITY	AVG	Small company	181.4	6	No load	1.12	-4.7	-6.6	0.2	71	
ENTERPRISE CAPITAL APPRECIATION	AVG	Maximum growth	101.2	-2	4.75	1.70†	-3.5	-4.8	0.0	71	
ENTERPRISE GROWTH 📈	AVG	Growth	88.4	-3	4.75	1.60†	-1.0	-2.4	0.0	113	
EUROPACIFIC GROWTH 📈	👑	Foreign	8269.5	43	5.75	0.99†	1.1	-0.5	1.5	71	
EV MARATHON GREATER CHINA GROWTH		Pacific	208.0	NM	5.00**	2.38†	-20.7	-20.8	0.6	71	
EV TRADITIONAL GROWTH (i)	👑👑	Growth	122.2	-12	4.75	0.95†	-4.4	-7.1	0.8	183	
EV TRADITIONAL INVESTORS	👑	Balanced	201.3	-6	4.75	0.93†	-1.8	-3.6	4.0	71	
EV TRADITIONAL STOCK (j)	👑	Growth/income	85.1	-5	4.75	0.98†	-4.1	-6.6	2.1	113	
EV TRADITIONAL TOTAL RETURN	👑	Utilities	448.7	-29	4.75	1.17†	-12.2	-13.5	5.1	23	
EVERGREEN 📈	👑👑	Small company	477.1	-24	No loadΔ	1.23	0.7	-3.7	0.5	28	
EVERGREEN FOUNDATION	👑👑👑	Balanced	331.6	38	No loadΔ	1.17	-1.1	-2.7	3.3	71	
EVERGREEN GLOBAL REAL ESTATE EQTY	👑👑	Specialty	98.1	-31	No loadΔ	1.54	-14.0	-15.2	0.8	71	
EVERGREEN GROWTH & INCOME (k)	👑	Growth/income	73.6	-6	No loadΔ	1.37	1.7	-0.4	0.9	293	
EVERGREEN LIMITED MARKET	👑	Small company	81.6	-21	No loadΔ	1.26	-10.5	-15.3	0.0	71	
EVERGREEN TOTAL RETURN 📈	AVG	Equity-income	944.4	-21	No loadΔ	1.18	-6.4	-8.5	6.2	71	
FAM VALUE	👑👑👑	Small company	210.3	-4	No load	1.37	6.8	5.8	0.6	71	
FIDELITY	👑	Growth/income	1886.1	22	No load	0.65	2.6	0.7	1.7	193	
FIDELITY ADVISOR EQUITY GROWTH A		Growth	908.2	113	4.75	1.82†	-0.9	-1.3	0.3	113	
FIDELITY ADVISOR EQUITY INCOME A		Equity-income	203.9	330	4.75	1.66†	6.5	5.4	1.8	71	
FIDELITY ADVISOR GLOB. RESEARCH A	AVG	Natural resources	193.2	240	4.75	2.07†	-2.3	-2.7	0.0	71	
FIDELITY ADVISOR GROWTH OPPORT A	👑👑	Growth	4826.6	106	4.75	1.62†	2.9	1.2	1.1	493	
FIDELITY ADVISOR INCOME & GRTH. A	👑👑	Balanced	3160.0	61	4.75	1.60†	-5.1	-5.8	2.3	71	
FIDELITY ADVISOR OVERSEAS A		Foreign	659.2	146	4.75	2.16†	2.0	1.8	0.0	71	
FIDELITY ADVISOR STRAT. OPPTY. A	AVG	Growth	376.7	22	4.75	1.84†	-7.1	-8.0	1.8	204	
FIDELITY ASSET MANAGER	👑👑👑	Asset allocation	11075.6	22	No load	1.04	-6.6	-7.7	2.9	71	
FIDELITY ASSET MANAGER: GROWTH		Asset allocation	2852.9	59	No load	1.15	-7.4	-8.1	1.5	71	
FIDELITY ASSET MANAGER: INCOME		Income	476.2	63	No load	0.71	-1.4	-2.8	4.7	71	
FIDELITY BALANCED	👑👑	Balanced	4999.1	7	No load	1.01	-5.3	-6.3	3.3	71	

* Incl. des. redemption fee. † Includes deferred sales charge. ‡ 12(b)-1 plan in effect. § Not currently accepting new accounts. ¶ Holding is less than 0.5% of assets.
 Δ For existing shareholders only. * New shareholders will have to pay sales charges. (d) Formerly Delaware Decatur I. (e) Formerly Delaware Decatur II. (f) Formerly Boston Company Appreciation Ret. (g) Formerly Dreyfus Strategic World Investing. (h) Formerly Boston Company Special Growth Ret. (i) Formerly Eaton Vance Growth. (j) Formerly Eaton Vance

ANNUAL TOTAL RETURNS (%)				TREND	PORTFOLIO DATA					RISK	TELEPHONE		
5 YEARS		1 YEAR		BW 10 YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		TOLL-FREE (800)	IN-STATE
PRETAX	AFTERTAX	PRETAX	AFTERTAX										
rated	7.2	6.3	13.2	11.7	High	0	5	LB	-8	Big Flower Press \$	Low	869-3863	NY 212-392-2550
					Very low	1	17	LB	20	Sprint(2)		869-3863	NY 212-392-2550
					High	3	18	MB	6	British Petroleum(2)		869-3863	NY 212-392-2550
rated					High	0	24	LV	3	Rite Aid(2)		869-3863	NY 212-392-2550
rated					High	0	29	SG	B	Idexx Laboratories(3)		869-3863	NY 212-392-2550
	8.2	6.0			Average	90	16	LV	0	WR Grace \$	Very low	869-3863	NY 212-392-2550
	3.8	2.1	9.9	8.2	Average	1	25	MB	2	Exxon(4)	Average	869-3863	NY 212-392-2550
					Low	1	27	MG	3	Hong Kong Telecommunications(2)		869-3863	NY 212-392-2550
	9.1	7.7			Low	7	32	MG	-1	American Barrick Resources(5)			NY 212-392-2550
					High	20	17	LB	3	Texaco(1)	Low	869-3863	NY 212-392-2550
	5.6	3.9			Low	1	16	LV	1	AT&T(2)	Low	869-3863	NY 212-392-2550
	8.1	7.6			Low	4	19	MB	13	CBS \$	Average	869-3863	NY 212-392-2550
	4.9	3.7	13.1	10.7	Average	11	28	MB	4	South America Fund(1)	Average	869-3863	NY 212-392-2550
	7.9	5.4	11.8	8.3	High	4	16	MV	2	MBNA(3)	Low	523-4640	PA 215-988-1333
	5.6	3.1	11.7	8.2	Average	2	19	LB	-3	WR Grace(3)	Average	523-4640	PA 215-988-1333
	6.4	3.9			High	2	19	LB	-1	Eastman Kodak(3)	Low	523-4640	PA 215-988-1333
	8.2	7.2			Low	9	23	MB	18	Columbia/HCA Healthcare(3)	High	523-4640	PA 215-988-1333
	12.1	9.8	15.4	13.2	Average	6	23	SB	6	Savoy Pictures Entertainment(2)	Very high	523-4640	PA 215-988-1333
	10.7	9.6			Low	31	17	SV	3	Geneva Steel Cl A(1)	Average	523-4640	PA 215-988-1333
rated					Very low	5	19	LB	5	Intl Flavors & Fragrances(4)		748-8500	
	9.8	8.1	14.0	11.3	Very low	4	16	LV	7	IBM(2)	Low	621-3979	CA 415-434-0311
	9.7	8.3	15.4	13.3	Very low	5	16	LV	23	Dayton Hudson(3)	Average	621-3979	CA 415-434-0311
	5.9	4.0	10.9	7.7	Average	17	15	LV	19	Chrysler(3)	Low	645-6561	NY 718-895-1206
	8.1	7.0	13.6	12.1	Very low	1	19	LG	11	Philip Morris(6)	Average	645-6561	NY 718-895-1206
rated					Average	14	21	LB	2	American Cyanamid(3)		645-6561	NY 718-895-1206
	8.2	5.5	12.2	8.6	High	17	23	LB	2	Merck(4)	Low	554-4611	NY 718-895-1396
	0.5	-1.3			Average	45	34	MG	-23	Newmont Mining(6)	Low	554-4611	NY 718-895-1396
	5.3	3.1	12.2	8.6	Average	3	15	LV	1	General Motors(3)	Average	645-6561	NY 718-895-1206
					Very low	2	13	MV	-25	Southern(5)		645-6561	NY 718-895-1206
	6.4	6.4			Very high	18	34	LB	15	Mitsubishi Heavy Industries(2)	Very low	645-6561	NY 718-895-1206
rated					Very high	29	25	MG	1	Homestake Mining(1)		554-4611	NY 718-895-1396
	5.3	2.6	10.9	7.4	Average	28	21	MB	-3	First Financial Management(3)		645-6561	NY 718-895-1206
					Very high	28	22	LB	-8	Schlumberger(4)	High	645-6561	NY 718-895-1206
rated						0	31	MB	-1	South African Breweries(1)		645-6561	NY 718-895-1206
	10.4	7.8			High	17	20	SV	7	Novacare(2)	Average	645-6561	NY 718-895-1206
	8.8	6.6	11.9	8.3	High	4	22	SB	-9	Global Marine(3)	High	645-6561	NY 718-895-1206
	5.9	6.0			Very high	72	18	SV	24	Granite Capital(3)	Average	645-6561	NY 718-895-1206
	6.9	4.9			Very high	21	22	MB	2	Deere(3)	Average	645-6561	NY 718-895-1206
	7.2	5.3	11.1	7.9	Average	15	16	MB	-2	AFLAC(3)	Average	645-6561	NY 718-895-1206
	8.8	5.6	11.7	8.9	Average	6	18	LB	8	Scott Paper(3)	Average	554-1156	
	8.8	6.8			Low	2	17	LV	6	Computer Associates Intl(2)	Very low	554-1156	
rated						1	18	SB	-2	Fuji Photo Film (ADR)(1)		554-1156	
	8.6	6.6			High	3	17	SV	3	IBP(1)	Average	872-2710	NY 404-631-0414
	12.3	11.9			High	8	25	LG	14	Motorola(5)	Average	432-4320	GA 404-396-8118
	10.1	7.5	13.4	10.0	Average	2	22	LG	14	Microsoft(5)	Average	432-4320	GA 404-396-8118
	10.7	9.8	17.6	15.9	Low	19	24	LB	11	Eurotunnel (Paris)(1)	Average	421-4120	CA 213-486-9200
rated					Low	2	23	MG	-4	HSBC Holdings(3)		225-6265	MA 617-482-8260
	5.3	2.8	11.2	8.3	High	8	21	LB	2	Reuters Holdings (ADR)(4)	High	225-6265	MA 617-482-8260
	7.3	4.5	10.7	6.9	Average	3	16	LV	11	Ford Motor(2)	Very low	225-6265	MA 617-482-8260
	5.5	2.1	11.7	7.9	High	1	17	LV	7	General Electric(3)	Low	225-6265	MA 617-482-8260
	4.9	1.9	11.4	7.8	Average	3	15	MV	1	PECO Energy(4)	Low	225-6265	MA 617-482-8260
	7.6	5.4	13.0	10.2	Low	4	17	SV	29	First Empire State(4)	Average	235-0064	NY 914-694-2020
	15.0	11.8			Average	9	16	MV	-3	General Electric(2)	Low	235-0064	NY 914-694-2020
	5.5	5.0			High	4	24	SB	-10	Horizon Outlet Centers(4)	High	235-0064	NY 914-694-2020
	9.8	8.0			Low	9	17	MB	20	Reynolds & Reynolds Cl A(4)	Average	235-0064	NY 914-694-2020
	7.9	5.1	13.4	10.7	High	2	14	SV	-17	Cameron Ashley(2)	Average	235-0064	NY 914-694-2020
	6.0	3.6	10.0	7.1	High	2	15	MV	-20	Bell Atlantic(5)	Low	235-0064	NY 914-694-2020
	13.3	12.5			Very low	7	19	SV	7	Fourth Financial(4)	Low	932-3271	NY 518-234-7000
	9.2	6.7	13.6	10.3	Very high	12	21	LB	4	British Petroleum (ADR)(2)	Low	544-8888	
rated					High	13	20	LG	-1	Compaq Computer(5)		522-7297	MA 617-439-6793
					High	20	17	LV	3	General Electric(3)		522-7297	MA 617-439-6793
rated					High	5	23	MB	-4	Phillips Petroleum(2)	Average	522-7297	MA 617-439-6793
	10.6	9.0			Average	12	18	LB	0	FNMA(5)	Average	522-7297	MA 617-439-6793
	15.2	13.6			Very high	37	29	MB	-4	Daiwa Securities(1)	Very low	522-7297	MA 617-439-6793
	10.1	8.2			Average	18	34	LV	2	Hoechst(1)		522-7297	MA 617-439-6793
	7.6	5.1			High	10	14	SV	-4	Bellsouth(4)	Low	522-7297	MA 617-439-6793
	11.1	9.2			High	28	21	LB	-3	FNMA(1)	Very low	544-8888	
					High	7	22	LB	-6	Intel(1)		544-8888	
rated					Average	28	20	LB	-5	Philip Morris \$		544-8888	
	9.0	6.7			High	28	30	MB	-6	Methanex(1)	Very low	544-8888	

DATA: MORNINGSTAR INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1994 RETURNS (%)				RANK OBJ
			ASSETS \$MIL	% CHG 1993-4	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE- TAX	AFTER- TAX	YIELD		
FIDELITY BLUE CHIP GROWTH	★★★	Growth	3287.0	200	3.00	1.22	9.9	9.2	0.0	23	
FIDELITY CANADA	★★★	Foreign	332.9	205	3.00	1.74	-12.0	-12.0	0.1	76	
FIDELITY CAPITAL APPRECIATION	AVG	Maximum growth	1623.2	14	3.00	1.24	2.5	-0.9	1.0	76	
FIDELITY CONTRAFUND	★★★	Growth	8682.4	40	3.00	1.03	-1.1	-1.3	0.0	1123	
FIDELITY DESTINY I	★★★	Growth	3207.8	2	8.24	0.70	4.4	-0.4	2.0	23	
FIDELITY DESTINY II	★★★	Growth	1468.2	17	8.24	0.80	4.5	0.9	1.8	23	
FIDELITY DISCIPLINED EQUITY	★★★	Growth	1160.1	46	No load	1.05	3.0	1.8	1.4	42	
FIDELITY DIVERSIFIED INTERNATIONAL		Foreign	306.0	28	3.00	1.36	1.1	0.1	0.3	7	
FIDELITY DIVIDEND GROWTH		Growth	102.4	15	No load	1.40	4.3	3.7	0.1	21	
FIDELITY EMERGING GROWTH		Maximum growth	635.2	-3	3.75*	1.11	-0.2	-0.7	0.0		
FIDELITY EMERGING MARKETS		Foreign	1508.3	-21	4.50*	1.55	-17.9	-18.0	0.2	76	
FIDELITY EQUITY-INCOME	★	Equity-income	7412.8	12	2.00	0.73	0.2	-2.6	3.0	3	
FIDELITY EQUITY-INCOME II		Equity-income	7697.5	53	No load	0.84	3.2	1.1	2.1	76	
FIDELITY EUROPE	★★	Europe	478.9	-3	3.00	1.31	6.3	5.8	1.0	7	
FIDELITY EUROPE CAPITAL APPREC		Europe	291.5	NM	3.00	1.70	6.9	6.9	0.0	7	
FIDELITY GLOBAL BALANCED		Income	236.5	-29	No load	1.67	-11.5	-11.7	0.9	7	
FIDELITY GROWTH & INCOME	★★	Growth/income	9344.9	22	3.00	0.82	2.3	0.1	1.8	21	
FIDELITY GROWTH COMPANY	★	Growth	2993.4	18	3.00	1.08	-2.2	-3.3	0.8	142	
FIDELITY INTL. GROWTH & INCOME	★★	Foreign	1272.6	19	No load	1.26	-2.9	-3.7	0.0	7	
FIDELITY JAPAN		Pacific	389.0	304	3.00	1.66	16.5	15.6	0.0	7	
FIDELITY LATIN AMERICA		Foreign	616.1	-23	4.50*	1.54	-23.2	-23.2	0.0	7	
FIDELITY LOW-PRICED STOCK	★★★	Small company	2354.5	14	4.50*	1.13	4.8	1.2	0.5	7	
FIDELITY MAGELLAN	★	Growth	36441.5	15	3.00	0.96	-1.8	-2.9	0.2	132	
FIDELITY MARKET INDEX		Growth/income	306.7	2	0.50*	0.45	1.0	0.3	2.3	41	
FIDELITY NEW MILLENNIUM		Growth	319.7	16	3.00	1.32	0.8	0.2	0.0	72	
FIDELITY OTC	★	Growth	1381.3	3	3.00	0.88	-2.7	-3.0	0.9	152	
FIDELITY OVERSEAS	★★	Foreign	2194.1	44	3.00	1.28	1.3	0.8	0.0	7	
FIDELITY PACIFIC BASIN	★★★	Pacific	475.5	-10	3.00	1.59	-2.8	-5.9	0.1	7	
FIDELITY PURITAN	★★★	Balanced	11769.4	31	2.00	0.79	1.8	-0.6	3.5	7	
FIDELITY REAL ESTATE INVESTMENT	★★★	Specialty	555.7	31	No load	1.18	2.0	0.6	4.8	5	
FIDELITY RETIREMENT GROWTH	★★★	Growth	3184.9	12	No load	1.12	0.1	-2.9	1.2	82	
FIDELITY SELECT AMERICAN GOLD	★★★	Precious metals	314.2	-14	3.75*	1.37	-15.5	-15.5	0.0	7	
FIDELITY SELECT BIOTECHNOLOGY	AVG	Health care	396.1	-29	3.75*	1.54	-18.2	-18.2	0.0	8	
FIDELITY SELECT CHEMICALS	★★★	Specialty	167.8	540	3.75*	1.52	14.8	14.0	0.7	1	
FIDELITY SELECT COMPUTERS	★★★	Technology	175.4	185	3.75*	1.70	20.5	20.5	0.0	7	
FIDELITY SELECT DEVELOPING COMM.		Technology	276.1	12	3.75*	1.57	15.1	12.7	0.0	7	
FIDELITY SELECT ELECTRONICS	★★★	Technology	156.6	243	3.75*	1.71	17.2	17.2	0.0	7	
FIDELITY SELECT ENERGY	★★★	Natural resources	96.7	17	3.75*	1.79	0.4	-0.7	0.7	7	
FIDELITY SELECT FINANCIAL SVCS.	AVG	Financial	94.2	-25	3.75*	1.63	-3.6	-6.4	1.2	5	
FIDELITY SELECT FOOD & AGRIC.	★★★	Specialty	85.5	-51	3.75*	1.71	6.1	4.3	0.2	3	
FIDELITY SELECT HEALTH CARE	★★★	Health care	796.1	39	3.75*	1.38	21.4	18.6	0.8	1	
FIDELITY SELECT HOME FINANCE	★★★	Financial	130.2	-18	3.75*	1.39	2.7	-1.8	0.5	1	
FIDELITY SELECT INDUSTRIAL EQUIP.	AVG	Technology	104.2	23	3.75*	1.69	3.1	2.9	0.0	7	
FIDELITY SELECT INDUSTRIAL MATER.	AVG	Natural resources	180.1	388	3.75*	1.61	8.2	7.9	0.8	7	
FIDELITY SELECT MEDICAL DELIVERY	★	Health care	247.6	65	3.75*	1.44	19.8	18.4	0.3	2	
FIDELITY SELECT NATURAL GAS		Natural resources	79.0	44	3.75*	1.75	-6.8	-6.9	0.2	7	
FIDELITY SELECT PAPER & FOREST	★★	Natural resources	76.3	58	3.75*	2.00	14.1	12.3	0.0	7	
FIDELITY SEL. PRECIOUS METALS	★★★	Precious metals	453.3	-18	3.75*	1.48	-1.1	-1.5	1.3	7	
FIDELITY SELECT REGIONAL BANKS	★★	Financial	108.4	-5	3.75*	1.50	0.2	-1.9	1.5	3	
FIDELITY SEL. SOFTWARE & COMP.	★★★	Technology	211.5	28	3.75*	1.50	0.4	0.1	0.0	7	
FIDELITY SELECT TECHNOLOGY	★★★	Technology	227.4	-1	3.75*	1.57	11.1	10.0	0.0	7	
FIDELITY SELECT TELECOMMUN.	AVG	Utilities	363.8	-12	3.75*	1.52	4.3	3.1	1.4	7	
FIDELITY SELECT UTILITIES GROWTH (I)	AVG	Utilities	202.4	-27	3.75*	1.37	-7.4	-8.8	3.1	7	
FIDELITY SMALL CAP STOCK		Small company	664.8	0	3.00	0.95	-3.3	-3.4	0.1	7	
FIDELITY SOUTHEAST ASIA		Pacific	660.9	-44	4.50*	1.55	-21.8	-21.8	0.0	7	
FIDELITY STOCK SELECTOR		Growth	786.7	26	No load	1.09	0.8	-0.7	0.8	72	
FIDELITY TREND	★★	Growth	1193.8	-14	No load	1.03	-6.7	-8.6	0.3	192	
FIDELITY UTILITIES (m)	★	Utilities	1079.6	-26	No load	0.88	-5.3	-7.9	3.9	7	
FIDELITY VALUE	★★★	Growth	3720.4	117	No load	1.11	7.6	5.9	0.4	12	
FIDELITY WORLDWIDE		World	703.9	107	3.00	1.40	3.0	1.4	0.5	7	
59 WALL ST EUROPEAN EQUITY		Europe	110.9	25	No load	1.50†	-3.9	-6.1	0.0	7	
59 WALL ST PACIFIC BASIN EQUITY		Pacific	120.6	30	No load	1.50†	-21.5	-24.9	0.0	7	
FIRST EAGLE FUND OF AMERICA	AVG	Growth	105.1	-3	1.00*	2.70	-2.6	-6.3	0.0	142	
FIRST INVESTORS BLUE CHIP	★★	Growth/income	121.0	4	6.25	1.58†	-3.0	-6.0	0.6	101	
FIRST INVESTORS GLOBAL	★★★	World	213.6	8	6.25	1.88†	-3.8	-4.7	0.5	7	
FIRST INVESTORS SPECIAL SITUATION		Small company	88.6	63	6.25	1.72†	-3.7	-5.1	0.0	7	
FIRST OMAHA EQUITY		Growth	145.2	20	No load	1.04†	7.4	5.8	2.1	12	
FIRST UNION BALANCED C INVESTMENT		Balanced	100.0	70	5.00**	1.39†	-3.0	-4.4	3.1	52	
FIRST UNION VALUE B INVESTMENT	AVG	Growth	188.4	1	4.75	0.92†	1.9	-0.4	2.9	52	
FLAG INVESTORS TELEPHONE INC. A	★★	Utilities	436.2	-7	4.50	0.92†	-6.3	-7.5	3.1	7	

* Includes redemption fee. † Includes deferred sales charge. ‡ 12(b)-1 plan in effect. § Not currently accepting new accounts. ¶ Holding is less than 0.5% of assets. (I) Formerly Fidelity Select International. (m) Formerly Fidelity Utilities Income.

Equity Funds

ANNUAL TOTAL RETURNS (%)				TREND	PORTFOLIO DATA						RISK	TELEPHONE			
5 YEARS PRETAX		5 YEARS AFTER TAX		10 YEARS PRETAX	10 YEARS AFTER TAX	BW 10 YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	INTL GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)	TOLL-FREE (800)	IN-STATE	
18.4	16.9						Very high	10	28	MG	7	Oracle Systems(3)	Low	544-8888	
3.6	2.8						Average	5	24	MB	-6	American Barrick Resources(5)	Average	544-8888	
8.1	5.4						High	16	27	MG	2	UAL(8)	Average	544-8888	
17.5	16.2	18.5	16.7				Very high	15	23	MB	3	Intel(2)	Low	544-8888	
15.4	11.5	17.4	13.1				Average	6	17	LB	6	FNMA(5)	Average	752-2347	MA 617-439-0547
16.1	12.9						Average	7	17	LB	3	FNMA(5)	Average	752-2347	MA 617-439-0547
12.4	10.6						High	4	16	LB	3	Chevron(3)	Average	544-8888	
							High	7	27	LV	5	Veba(2)		544-8888	
							Very high	17	24	SG	7	LM Ericsson Telephone (ADR)(4)		544-8888	
							Very high	4	24	MG	10	Compaq Computer(5)		544-8888	
							Very high	3	30	MG	-4	Telefonos De Mexico L (ADR)(2)		544-8888	
9.2	7.2	12.5	9.2				Average	6	18	LV	8	General Electric(3)	Low	544-8888	
							Average	12	19	LV	1	British Petroleum (ADR)(3)		544-8888	
5.5	4.9						Average	3	20	MB	13	Nokia Free(4)	High	544-8888	
							Very high	7	27	MV	-6	Philips Electronics(5)		544-8888	
							Very high	19	29	MG	11	Sherritt(1)		544-8888	
12.5	10.1						High	12	19	LB	6	General Electric(3)	Low	544-8888	
13.5	11.9	17.0	14.9				High	5	20	LB	3	Compaq Computer(5)	High	544-8888	
5.8	5.1						Very high	9	34	LV	1	Koninklijke PTT(2)	Average	544-8888	
							Very high	6	46	MB	-1	Matsushita Electric Indl(3)		544-8888	
							High	8	21		-18	Grupo Carso CI A1(5)		544-8888	
18.9	16.4						Average	25	14	SV	8	Welsh Water plc(1)	Low	544-8888	
12.0	9.3	18.0	14.9				High	3	21		9	Motorola(2)	Average	544-8888	
							Very low	0	19	LB	17	General Electric(2)		544-8888	
							Very high	8	23	MG	9	Herman Miller(4)		544-8888	
							Very high	12	22	MG	6	Intel(4)	Average	544-8888	
5.0	3.3	19.2	16.8				Average	13	31	LV	9	Deutsche Bank(1)	High	544-8888	
3.8	2.9						High	1	38	MG	9	Nomura Securities(2)	Very high	544-8888	
10.7	7.9	13.7	10.0				Average	6	23	MB	1	Schlumberger(2)	Low	544-8888	
11.8	10.2						Average	8	24	SB	0	Equity Residential Ppty Tr(6)	Low	544-8888	
12.1	8.9	15.7	12.0				Average	26	20	MB	4	IBM(2)	Average	544-8888	
2.6	2.6						Low	11	31	MG	-3	American Barrick Resources(10)	Very high	544-8888	
16.2	14.8						Average	27	30	SG	-14	Genentech(9)	Very high	544-8888	
13.4	11.4						Average	6	20	MB	3	Union Carbide(7)	Average	544-8888	
24.0	23.2						Very high	7	18	MG	9	Advanced Micro Devices(8)	Very high	544-8888	
							Very high	8	31	MG	13	DSC Communications(9)		544-8888	
23.1	22.0						Very high	6	17	MB	-1	Intel(10)	High	544-8888	
2.2	0.9	8.5	7.3				High	10	27	MB	0	British Petroleum (ADR)(9)	High	544-8888	
14.6	12.4	13.6	12.0				Average	6	10	MV	-7	Bank of New York(7)	Very high	544-8888	
12.4	10.5						High	14	16	MG	9	Philip Morris(10)	Low	544-8888	
18.6	15.7	21.5	19.8				Very high	12	22	LG	7	Pfizer(10)	High	544-8888	
23.6	21.8						High	10	11	SV	0	Standard Federal Bank (MI)(4)	High	544-8888	
12.0	11.7						High	5	18	SV	-4	Caterpillar(10)	High	544-8888	
10.7	10.3						High	10	24	MG	-7	Union Carbide(9)	Average	544-8888	
17.8	16.5						Very high	17	22	MG	9	US Healthcare(11)	Very high	544-8888	
							High	2	25	MB	-16	Burlington Resources(5)		544-8888	
11.6	11.0						Very high	3	24	MB	1	Stone Container(7)	High	544-8888	
5.6	5.1	8.0	7.2				Low	12	28	MG	3	American Barrick Resources(8)	Very high	544-8888	
16.8	14.3						High	3	8	MV	-7	NationsBank(7)	High	544-8888	
21.6	19.3						High	9	27	MG	6	Cabletron Systems(8)	Very high	544-8888	
22.3	20.8	10.6	9.7				High	5	22	LG	17	Intel(7)	High	544-8888	
11.3	10.0						High	8	22	LG	2	Ameritech(9)	Average	544-8888	
7.0	4.7	12.9	11.0				Low	3	16	LV	-8	Ameritech(6)	Low	544-8888	
							High	16	20	SB	1	Atmel(3)		544-8888	
							Very high	2	25	MG	-1	Hutchison Whampoa(4)		544-8888	
							Very high	4	18	LB	1	Philip Morris(3)		544-8888	
9.1	7.4	13.4	10.7				Low	5	23	MG	11	Golden West Financial(4)	High	544-8888	
8.4	6.1						High	10	18	MV	0	Ameritech(4)	Low	544-8888	
12.0	10.6	13.6	12.1				Very high	5	22	MB	2	British Petroleum (ADR)(2)	Low	544-8888	
							Average	32	25	MV	-1	Grupo Tribasa (ADR)(1)		544-8888	
							Average	2	20	MV	-1	Cable & Wireless(2)			MA 212-493-8100
							Average	14	23	LB	-7	New World Development(4)			MA 212-493-8100
8.4	5.9						High	3	17	MV	8	Tejas Gas(6)	Average	451-3623	NY 212-943-9200
6.5	5.1						Average	6	18	LB	2	Motorola(5)	Average	423-4026	NY 212-858-8000
2.9	2.5	14.4	13.0				Average	6	25	LB	1	Broken Hill Proprietary(2)	High	423-4026	NY 212-858-8000
							Average	13	23	SG	3	Newbridge Networks(2)		423-4026	NY 212-858-8000
							Low	17	21	LB	7	Becton Dickinson(4)		662-4203	
								10	16	LV	1	Phelps Dodge(1)		326-3241	PA 704-374-4343
7.6	5.6						Average	3	18	LV	1	National City(3)	Low	326-3241	PA 704-374-4343
7.2	5.7	15.4	12.4				Very low	2	19	LB	18	AT&T(6)	Average	767-3524	

DATA: MORNINGSTAR INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1994 RETURNS (%)				RANK
			ASSETS \$MIL	% CHG 1993-4	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD		
FLAG INVESTORS VALUE BUILDER A		Balanced	136.2	14	4.50	1.35†	-0.4	-1.3	3.1		
FLEX-FUNDS MUIRFIELD	◆◆◆	Asset allocation	81.8	26	No load	1.25†	2.7	1.8	2.6		
FORTIS ADVANTAGE ASSET ALLOC A	◆	Asset allocation	116.3	5	4.50	1.53†	-0.8	-1.8	2.8		
FORTIS ADVANTAGE CAPITAL APPR. A	◆◆◆	Small company	68.9	17	4.50	1.57†	-7.2	-7.2	0.0		
FORTIS CAPITAL A	◆	Growth	237.7	-3	4.75	1.21†	2.5	1.2	0.3	42	
FORTIS GROWTH A	◆◆	Growth	545.3	-8	4.75	1.09†	-8.2	-8.7	0.0	212	
FORTRESS UTILITY	◆	Utilities	781.1	-21	2.00*	1.11	-7.9	-9.4	5.4		
FOUNDERS BALANCED	◆◆	Balanced	96.0	32	No load	1.33†	-1.9	-2.6	2.3		
FOUNDERS BLUE CHIP	AVG	Growth/income	312.2	2	No load	1.24†	0.5	-1.1	0.9	5	
FOUNDERS DISCOVERY	◆◆	Small company	187.5	-17	No load	1.63†	-7.7	-7.7	0.0		
FOUNDERS FRONTIER	AVG	Small company	249.2	-2	No load	1.63†	-2.8	-3.5	0.0		
FOUNDERS GROWTH	AVG	Growth	310.1	-10	No load	1.30†	-3.3	-4.1	0.0	162	
FOUNDERS SPECIAL	AVG	Maximum growth	300.9	-30	No load	1.35†	-4.9	-5.9	0.0		
FOUNDERS WORLDWIDE GROWTH	◆◆◆	World	104.9	24	No load	1.70†	-2.2	-2.9	0.0		
FPA CAPITAL	◆	Small company	180.8	22	6.50	1.03	10.4	8.4	0.2		
FPA PARAMOUNT	◆◆	Growth/income	463.8	37	6.50	0.90	9.4	6.0	1.6		
FRANKLIN BALANCE SHEET INVESTMENT		Growth	137.4	411	1.50	0.76†	1.5	0.8	1.0	52	
FRANKLIN DYNATECH	◆	Technology	69.5	-1	4.50	1.00†	5.2	4.7	0.5		
FRANKLIN EQUITY	◆◆	Growth	281.2	-13	4.50	0.79†	-1.3	-4.2	1.1	122	
FRANKLIN EQUITY-INCOME	◆	Equity-income	92.7	105	4.50	0.44†	-0.3	-2.2	4.6		
FRANKLIN GLOBAL UTILITIES		Utilities	121.8	73	4.50	0.84†	-8.9	-10.6	3.1		
FRANKLIN GOLD	◆◆◆	Precious metals	379.1	10	4.50	0.81†	-4.7	-5.0	1.0		
FRANKLIN GROWTH	AVG	Growth	523.4	-7	4.50	0.77†	2.9	2.6	0.9	42	
FRANKLIN INCOME	◆◆	Income	4882.5	17	4.25	0.64†	-6.4	-9.1	8.5		
FRANKLIN RISING DIVIDENDS	◆	Growth/income	241.4	-30	4.50	1.43†	-5.2	-5.7	1.9	121	
FRANKLIN UTILITIES	◆	Utilities	2569.8	-26	4.25	0.64†	-11.7	-13.3	6.2		
FREMONT GLOBAL	◆	Asset allocation	436.8	104	No load	0.95	-4.2	-4.7	1.0		
FT INTERNATIONAL EQUITY A	◆◆◆	Foreign	261.1	35	5.50	1.60†	0.5	-0.9	0.0		
FUNDAMENTAL INVESTORS	AVG	Growth/income	2611.1	32	5.75	0.65†	1.3	-0.1	2.5	3	
G.T. GLOBAL AMERICA GROWTH A (n)	AVG	Small company	199.9	68	4.75	1.66†	15.7	12.3	0.1		
G.T. GLOBAL EMERGING MARKETS A		Foreign	333.8	17	4.75	2.09†	-3.8	-5.0	0.0		
G.T. GLOBAL EUROPE GROWTH A (o)	◆◆◆	Europe	647.3	-24	4.75	1.74†	-5.8	-6.3	0.5		
G.T. GLOBAL GROWTH & INCOME B		World	348.2	66	5.00**	2.34†	-4.2	-5.2	3.0		
G.T. GLOBAL HEALTH CARE A	◆	Health care	387.5	-15	4.75	1.96†	0.3	-1.7	0.0		
G.T. GLOBAL INTL. GRTH. A (p)	◆◆◆	Foreign	431.0	-18	4.75	1.71†	-7.8	-10.3	0.0		
G.T. GLOBAL JAPAN GROWTH A (q)	◆◆◆	Pacific	100.3	13	4.75	1.99†	6.6	6.0	0.0		
G.T. GLOBAL NEW PACIFIC GROWTH A (r)	◆◆◆	Pacific	405.9	-19	4.75	1.81†	-19.7	-20.8	0.0		
G.T. GLOBAL TELECOMMUNICATIONS A		Utilities	1481.0	7	4.75	1.83†	-4.4	-5.8	0.0		
G.T. GLOBAL WORLDWIDE GROWTH A (s)	◆◆	World	182.2	-6	4.75	1.78†	-6.7	-7.9	0.0		
G.T. LATIN AMERICA GROWTH A		Foreign	283.1	41	4.75	2.14†	-6.6	-8.6	0.0		
GABELLI ASSET	◆◆	Growth	979.3	6	No load	1.33†	-0.2	-1.6	4.7	92	
GABELLI GLOBAL TELECOMMUNICATIONS		Utilities	138.9	331	4.50	2.00†	-3.7	-4.0	0.7		
GABELLI GROWTH	AVG	Growth	493.2	-27	No load	1.41†	-3.4	-6.8	0.4	162	
GABELLI SMALL CAP GROWTH		Small company	196.5	-5	4.50	1.54†	-2.9	-4.6	0.0		
GABELLI VALUE	◆	Growth	441.4	-10	5.50	1.52†	0.0	-3.7	0.8	92	
GALAXY ASSET ALLOCATION RETAIL		Asset allocation	67.7	-39	No load	1.18	-2.5	-3.3	2.8		
GALAXY EQUITY GROWTH RETAIL		Growth	68.1	-84	No load	0.90	0.6	-0.1	1.2	72	
GALAXY EQUITY VALUE RETAIL	◆	Growth	73.6	-60	No load	1.03	3.5	0.4	1.4	32	
GALAXY II LARGE COMPANY INDEX RET. (t)		Growth/income	137.8	-8	No load	0.40	1.0	-0.4	2.5	42	
GALAXY II SMALL COMPANY INDEX RET. (u)		Small company	230.7	-13	No load	0.40	-3.7	-5.4	1.6		
GAM INTERNATIONAL	◆	Foreign	159.4	98	5.00	1.58	-10.2	-15.9	3.1		
GATEWAY INDEX PLUS	◆◆◆	Growth/income	161.1	-23	No load	1.11	5.6	3.3	1.6		
GEORGE PUTNAM FUND OF BOSTON A	◆	Balanced	895.9	9	5.75	0.95†	-0.4	-2.3	4.3		
GINTEL	◆◆	Growth	88.3	-35	No load	2.20	-16.5	-16.8	0.4	232	
GLOBAL UTILITY B		Utilities	254.5	6	5.00**	1.95†	-8.6	-9.9	2.6		
GOLDMAN SACHS CAPITAL GROWTH		Growth	862.7	11	5.50	1.37†	-1.1	-4.1	0.1	112	
GOLDMAN SACHS GROWTH & INCOME		Growth/income	169.5	465	5.50	1.25†	5.9	4.7	1.7		
GOLDMAN SACHS INTL. EQUITY		Foreign	312.8	67	5.50	1.76†	-6.9	-7.8	0.0		
GOLDMAN SACHS SELECT EQUITY		Growth/income	91.3	6	5.50	1.28†	1.3	-0.8	1.3	32	
GOLDMAN SACHS SMALL CAP EQUITY		Small company	352.4	88	5.50	1.39†	-14.8	-16.1	0.0		
GOV'TT EMERGING MARKETS		Foreign	91.0	73	4.95	2.18†	-12.7	-16.5	0.0		
GRADISON-MCDONALD ESTAB. VALUE	AVG	Growth	260.2	7	No load	1.20†	0.2	-1.0	1.4	82	
GRADISON-MCDONALD OPPORT. VALUE	AVG	Small company	82.9	-1	No load	1.38†	-2.2	-3.1	0.7		
GROWTH FUND OF AMERICA	AVG	Growth	5274.2	4	5.75	0.78†	0.0	-1.3	0.6	92	
GROWTH FUND OF AMERICA	◆	Growth	640.7	14	4.50	0.84†	-1.4	-2.8	1.1	122	
HANCOCK CAPITAL GROWTH A (v)	◆◆◆	Maximum growth	68.6	-20	5.75	1.46†	-11.3	-12.0	0.0		
HANCOCK EMERGING GROWTH B (w)	AVG	Small company	268.4	21	5.00**	2.28†	-1.5	-1.5	0.0		
HANCOCK FREEDOM GLOBAL A		World	95.2	9	5.00	2.01†	-4.9	-7.6	0.0		
HANCOCK FREEDOM REGIONAL BANK B	◆◆◆	Financial	484.8	186	5.00**	2.01†	-0.2	-1.1	1.2		
HANCOCK GROWTH & INCOME A (x)	◆	Growth/income	114.5	-6	5.75	1.31†	-8.5	-9.1	2.3	132	

* Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts. § Holding is less than 0.5% of assets.

(n) Formerly G.T. America Growth A. (o) Formerly G.T. Europe Growth A. (p) Formerly G.T. International Growth A. (q) Formerly G.T. Japan Growth A. (r) Formerly G.T. Pacific Growth A. (s) Formerly G.T. Worldwide Growth A. (t) Formerly IBM Large Company Index. (u) Formerly IBM Small Company Index. (v) Formerly Transamerica Capital Growth A. (w) Formerly Transamerica Special Emerging Grth B. (x) Formerly Transamerica Growth & Income A.

Equity Funds

ANNUAL TOTAL RETURNS (%)				TREND	PORTFOLIO DATA						RISK	TELEPHONE	
5 YEARS	10 YEARS	BW 10-YEAR			TURNOVER	%CASH	P-E	STYLE	UNTAXED	LARGEST HOLDING		TOLL-FREE	IN-STATE
PRETAX	PRETAX	ANALYSIS					RATIO		GAINS (%)	COMPANY (% ASSETS)		(800)	
rated					Very low	5	16	LB	2	Conseco(2)		767-3524	
9.7	6.4				Very high	30	NA	MB	0	Fidelity Capital Appreciation(6)	Very low	325-3539	OH 614-766-7000
8.5	7.0				High	1	24	MG	10	Oracle Systems(2)	Low	800-2638	MN 612-738-4000
10.2	9.7				Average	28	31	SG	26	Input/Output(4)	Very high	800-2638	MN 612-738-4000
8.7	6.6	13.8	11.5		Average	6	25	MG	26	Oracle Systems(5)	Average	800-2638	MN 612-738-4000
9.9	8.2	14.8	13.1		Low	18	28	MG	32	Oracle Systems(5)	Very high	800-2638	MN 612-738-4000
8.0	6.0				Low	5	16	MV	-5	British Telecom (ADR)(4)	Very low	245-5051	PA 412-288-1900
8.1	6.2	10.5	7.7		Very high	12	15	LV	-1	Gap(2)	Very low	525-2440	CO 303-394-4404
8.2	4.8	13.3	8.6		Very high	20	18	MB	5	Gap(3)	Low	525-2440	CO 303-394-4404
16.7	16.2				High	29	23	SB	11	Sterling Software(2)	High	525-2440	CO 303-394-4404
11.3	10.2				High	33	23	SG	13	Maxim Integrated Products(2)	High	525-2440	CO 303-394-4404
10.8	9.0	15.5	12.8		High	24	20	MB	8	FNMA(3)	High	525-2440	CO 303-394-4404
11.9	8.7	14.8	11.7		Very high	25	20	MB	6	Texas Instruments(3)	High	525-2440	CO 303-394-4404
13.2	12.6				High	26	25	MG	11	Nokia(4)	Low	525-2440	CO 303-394-4404
17.3	14.8	18.1	15.3		Low	2	13	SV	35	Green Tree Financial(9)	Very high	982-4372	CA 310-473-0225
12.9	9.2	15.2	11.1		Average	21	31	MG	10	Occidental Petroleum(5)	Low	982-4372	CA 310-473-0225
10.5	9.5	11.8	10.3		Low	11	13	SV	1	USLife(4)		342-5236	CA 415-312-2000
5.1	2.7	11.4	8.8		Very low	31	23	LG	38	Motorola(11)	Average	342-5236	CA 415-312-2000
9.2	7.0				High	5	18	MB	0	Chevron(2)	Average	342-5236	CA 415-312-2000
					Low	22	20	LB	-1	American Home Products(2)	Low	342-5236	CA 415-312-2000
rated					Low	12	15	LV	-10	Veba(3)		342-5236	CA 415-312-2000
2.4	1.6	9.7	8.3		Very low	8	35	MG	22	American Barrick Resources(12)	Very high	342-5236	CA 415-312-2000
8.0	7.2	13.2	12.1		Very low	4	22	LB	25	Computer Sciences(4)	Low	342-5236	CA 415-312-2000
11.1	7.7	11.9	7.8		Low	16	14	LV	-5	Bristol-Myers Squibb(1)	Very low	342-5236	CA 415-312-2000
6.6	5.9				Low	11	15	MV	-4	Philip Morris(3)	Low	342-5236	CA 415-312-2000
6.0	4.0	10.5	7.8		Very low	2	15	MV	-7	Southern(4)	Low	342-5236	CA 415-312-2000
7.0	5.8				Low	8	25	LG	4	HSBC Holdings(1)	Very low	548-4539	CA 415-768-9000
3.4	2.8	15.5	12.9		Average	4	33	LB	10	DDI(2)	High	245-5051	PA 412-288-1900
10.0	7.5	14.8	11.6		Low	8	17	LB	12	Time Warner(3)	Average	421-4120	CA 415-421-9360
12.8	11.2				High	30	19	SB	8	Haggar(3)	High	824-1580	CA 415-392-6181
rated					High	4	31	MG	8	Brasileiras(3)		824-1580	CA 415-392-6181
-0.9	-1.2				High	8	23	LV	-25	Volkswagen(3)	High	824-1580	CA 415-392-6181
rated					High	9	18	LV	3	Elektrowatt (BR)(2)		824-1580	CA 415-392-6181
9.7	9.0				Average	9	28	MG	16	Roche Holding (GEN)(6)	High	824-1580	CA 415-392-6181
2.5	1.7				High	6	30	MG	5	Autobacs Seven(3)	High	824-1580	CA 415-392-6181
-5.0	-5.3				Low	1	48	MG	11	Nakamichi(5)	Very high	824-1580	CA 415-392-6181
3.6	2.3	15.7	12.5		High	8	23	MB	2	State Street Boston(6)	High	824-1580	CA 415-392-6181
rated					Average	6	26	LG	5	Telebras Pn(4)		824-1580	CA 415-392-6181
5.3	4.5				High	9	29	LB	7	Canon(2)	Average	824-1580	CA 415-392-6181
					High	3	25	MG	-2	Grupo Industrial Alfa CI A(4)		824-1580	CA 415-392-6181
9.2	7.9				Low	16	20	MG	18	American Cyanamid(4)	Low	422-3554	NY 914-921-5100
rated						12	26	LG	-4	Airtouch Commun.(4)		422-3554	
8.1	6.6				Average	2	22	MG	11	Genentech(3)	Average	422-3554	NY 914-921-5100
					Low	1	22	SB	14	Pittway CI A(3)		422-3554	NY 914-921-5100
11.3	8.6				Low	8	16	MB	10	Media General CI A(14)	Average	422-3554	NY 914-921-5100
					Very low	3	18	LB	-1	Citicorp(3)		628-0414	
					Low	10	21	LB	50	Mobil(3)		628-0414	
8.9	6.8				Average	15	15	LV	25	Becton Dickinson(2)	Low	628-0414	
					Very low	4	18	LB	12	General Electric(2)		628-0414	
					Low	0	19	MB	6	Microsoft(1)		628-0414	
12.3	8.8				High	18	40	LG	-6	Northern Ireland Electric(2)	Average	426-4685	NY 212-407-4600
9.1	6.4	10.6	7.7		Low	0	17	LB	6	General Electric(6)	Very low	354-6339	OH 513-248-2700
7.7	5.1	12.4	8.8		High	4	16	LV	-1	JP Morgan(1)	Very low	225-1581	MA 617-292-1000
3.5	1.8	9.0	6.3		Average	13	22	SB	-1	FNMA(12)	High	243-5808	CT 203-622-6400
					Very low	1	15	LV	0	AT&T(4)		225-1852	
rated					Low	7	20	MB	7	National Medical Enterprises(5)		762-5035	
rated						4	20	MV	-2	National Medical Enterprises(4)		526-7384	
					Average	1	17	SG	1	Wolters Kluwer(7)		526-7384	
rated					High	1	16	LB	5	PECO Engery(4)		762-5035	
					Average	6	18	SV	-15	American Publishing CI A(4)		526-7384	
rated					High	3	22		-8	Telefonos De Mexico CI L(2)		634-6838	CA 415-391-7494
8.4	7.1	13.6	11.6		Average	30	15	MV	19	Andrew(3)	Average	869-5999	OH 513-579-5700
8.0	6.7	11.9	10.6		Average	30	15	SV	15	Michaels Stores(3)	Average	869-5999	OH 513-579-5700
9.9	8.4	14.7	12.6		Low	18	22	LG	23	Time Warner(4)	Average	421-4120	CA 415-421-9360
11.1	9.2	15.2	12.0		Average	6	16	MV	12	IBM(3)	Average	221-3253	
5.1	3.9				High	2	19	MB	4	Millipore(4)	Very high	225-5291	
14.2	14.1				Low	3	22	SB	18	3Com(1)	High	225-5291	
rated					High	1	28	LG	15	Coca-Cola(2)		225-5291	
18.2	16.2				Low	10	10	MV	2	Mercantile Bancorp(3)	Average	225-5291	
7.0	5.2	10.9	8.0		Very high	0	17	LB	0	Northrop Grumman(4)	Average	225-5291	

DATA: MORNINGSTAR INC., CHICAGO, IL.

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MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1994 RETURNS (%)				RANK OBJ
			ASSETS \$MIL	% CHG 1993-4	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE- TAX	AFTER- TAX	YIELD		
HANCOCK GROWTH A	◆	Growth	145.8	-20	5.00	1.64†	-7.6	-7.9	0.0	209	
HANCOCK SOVEREIGN ACHIEVERS B	◆◆	Growth	88.5	-8	5.00**	2.15†	-6.0	-7.3	0.2	192	
HANCOCK SOVEREIGN BALANCED B		Balanced	78.7	7	5.00**	1.91†	-4.2	-5.5	4.4	4	
HANCOCK SOVEREIGN INVESTORS A	◆◆◆	Growth/income	1081.0	-12	5.00	1.17†	-1.9	-3.0	3.2	93	
HANCOCK SPECIAL EQUITIES A	◆◆◆	Small company	303.8	10	5.00†	1.63†	2.0	2.0	0.0	2	
HANCOCK SPECIAL OPPORTUNITIES B		Growth	128.3	394	5.00**	2.22†	-9.4	-9.4	0.0	224	
HARBOR CAPITAL APPRECIATION	◆	Growth	226.9	59	No load	0.85	3.4	3.0	0.2	33	
HARBOR GROWTH	◆◆	Growth	132.6	-31	No load	0.89	-11.4	-12.1	0.0	230	
HARBOR INTERNATIONAL	AVG	Foreign	2982.2	33	No load†	1.16	5.4	4.0	1.0		
HARBOR INTERNATIONAL GROWTH		Foreign	71.8	754	No load	0.97	-7.7	-7.9	0.6	5	
HEARTLAND VALUE	◆◆◆	Small company	325.0	82	No load	1.49†	1.7	0.7	0.0	2	
HERITAGE CAPITAL APPRECIATION	AVG	Growth	69.5	-10	4.00	1.55†	-2.4	-4.7	0.4	144	
HIGHMARK INCOME-EQUITY FID	AVG	Equity-income	202.7	-4	No load	1.06	-0.6	-2.7	3.6	1	
HOMESTEAD VALUE		Growth/income	90.1	71	No load	1.25	2.5	1.7	2.0	21	
HOTCHKIS & WILEY EQUITY-INCOME (y)	◆	Equity-income	106.7	29	No load	1.00	-3.5	-5.0	3.0	2	
IAI EMERGING GROWTH		Small company	292.9	33	No load	1.25†	0.2	-1.1	0.0	3	
IAI GROWTH & INCOME	◆	Growth/income	106.1	-17	No load	1.25†	-4.8	-6.3	0.8	121	
IAI INTERNATIONAL	◆◆	Foreign	157.3	50	No load	1.74†	-0.1	-1.9	0.0	2	
IAI MIDCAP GROWTH		Growth	75.4	104	No load	1.25†	5.7	4.4	0.0	19	
IAI REGIONAL	AVG	Growth	513.2	-20	No load	1.23†	0.7	-1.2	0.9	76	
IDEX	◆◆	Growth	270.2	-21	8.50	1.29	-7.6	-8.1	0.6	210	
IDEX 3	◆◆	Growth	143.3	-25	8.50†	1.24	-7.4	-7.8	0.8	207	
IDEX II GLOBAL A		World	84.3	223	5.50	2.14†	0.9	-0.1	0.0	1	
IDEX II GROWTH A	◆	Growth	412.4	-21	5.50	1.76†	-8.3	-8.5	0.0	219	
IDS BLUE CHIP ADVANTAGE		Growth/income	146.9	3	5.00	0.91	1.2	-1.4	1.8	37	
IDS DISCOVERY	◆	Small company	647.0	23	5.00	0.97	-7.8	-7.8	0.0	8	
IDS DIVERSIFIED EQUITY-INCOME		Equity-income	945.9	52	5.00	0.87	-3.7	-5.7	2.8	2	
IDS EQUITY PLUS	◆	Growth/income	580.4	-10	5.00	0.72	-8.0	-9.4	1.0	133	
IDS GLOBAL GROWTH		World	640.4	97	5.00	1.38	-7.3	-7.7	0.7	4	
IDS GROWTH	AVG	Growth	1007.0	2	5.00	0.83	2.9	0.5	0.2	43	
IDS INTERNATIONAL	◆◆	World	769.8	51	5.00	1.30	-2.2	-3.9	0.2	2	
IDS MANAGED RETIREMENT	◆	Growth/income	2248.7	15	5.00	0.81	-4.6	-6.9	1.2	120	
IDS MUTUAL	◆◆	Balanced	2924.8	1	5.00	0.79	-3.0	-5.6	4.9	3	
IDS NEW DIMENSIONS	◆◆	Growth	4458.4	19	5.00	0.90	-3.0	-4.2	0.9	156	
IDS PRECIOUS METALS	◆◆◆	Precious metals	69.8	-5	5.00	1.51	-9.6	-9.7	0.5	1	
IDS PROGRESSIVE	◆	Growth	278.0	4	5.00	1.09	1.4	-0.4	1.8	61	
IDS STOCK	◆	Growth/income	2259.2	7	5.00	0.76	-2.8	-6.0	3.3	99	
IDS STRATEGY AGGRESSIVE EQUITY	◆◆	Maximum growth	726.0	8	5.00**	1.71†	-6.9	-7.2	0.0	2	
IDS STRATEGY EQUITY	◆	Growth/income	1192.3	18	5.00**	1.56†	-3.3	-5.2	2.0	108	
IDS STRATEGY WORLDWIDE GROWTH	◆◆◆	World	316.6	93	5.00**	2.45†	-2.8	-3.2	0.0	2	
IDS UTILITIES INCOME	AVG	Utilities	585.9	-26	5.00	0.82	-8.5	-10.2	3.6	1	
INCOME FUND OF AMERICA	◆	Income	10502.7	2	5.75	0.63†	-2.5	-4.5	6.3		
INTERNATIONAL EQUITY	◆◆	Foreign	174.6	-49	No load	1.03	-0.3	-3.5	0.0	2	
INVESCO DYNAMICS	◆◆	Maximum growth	313.0	1	No load	1.17†	-1.9	-7.0	0.0	1	
INVESCO EMERGING GROWTH	◆◆	Small company	171.1	-19	No load	1.37†	-3.7	-9.5	0.0	6	
INVESCO EUROPEAN	◆◆	Europe	272.4	12	No load	1.28	-3.0	-3.4	1.3		
INVESCO GROWTH	AVG	Growth	457.9	-8	No load	1.03†	-8.8	-11.5	0.7	223	
INVESCO INDUSTRIAL INCOME	◆◆	Equity-income	3768.1	1	No load	0.92†	-3.9	-6.3	3.7	2	
INVESCO INTERNATIONAL GROWTH	◆◆◆	Foreign	119.2	30	No load	1.43	0.6	-1.1	0.5	1	
INVESCO PACIFIC BASIN	◆◆◆	Pacific	272.1	9	No load	1.26	4.7	1.3	0.3		
INVESCO STRATEGIC FINCL. SERVICES	◆◆◆	Financial	239.7	-28	No load	1.03	-5.9	-6.6	2.4		
INVESCO STRATEGIC GOLD	◆◆	Precious metals	208.7	-26	No load	0.97	-27.9	-27.9	0.0	1	
INVESCO STRATEGIC HEALTH SCIENCE	AVG	Health care	473.7	-16	No load	1.16	0.9	0.9	0.0		
INVESCO STRATEGIC LEISURE	◆◆◆	Specialty	271.8	-12	No load	1.14	-5.0	-6.1	0.0		
INVESCO STRATEGIC TECHNOLOGY	◆◆◆	Technology	312.2	25	No load	1.13	5.3	4.3	0.0	1	
INVESCO STRATEGIC UTILITIES	AVG	Utilities	126.4	-28	No load	1.06	-9.9	-10.9	3.4	1	
INVESTMENT COMPANY OF AMERICA	AVG	Growth/income	19279.6	1	5.75	0.59†	0.2	-1.6	2.6	58	
IVY GROWTH A	◆	Growth	229.9	-11	5.75	1.37†	-3.1	-4.6	0.8	158	
IVY INTERNATIONAL A	◆	Foreign	228.5	53	5.75	1.64†	3.9	2.6	0.9		
JANUS	◆◆	Growth	9400.6	2	No load	0.92	-1.1	-1.7	0.0	117	
JANUS BALANCED		Balanced	93.4	21	No load	1.41	-0.8	-2.0	4.0	1	
JANUS ENTERPRISE		Growth	354.1	37	No load	1.24	8.9	7.7	2.2	11	
JANUS GROWTH & INCOME		Growth/income	456.5	-11	No load	1.21	-4.9	-5.1	0.7	122	
JANUS MERCURY		Growth	690.1	444	No load	1.48	15.9	15.2	1.2	3	
JANUS TWENTY	AVG	Growth	2504.3	-29	No load†	1.04	-6.7	-6.8	0.3	197	
JANUS VENTURE	◆◆	Small company	1496.1	-16	No load†	0.96	5.5	3.8	0.1	1	
JANUS WORLDWIDE	◆◆◆	World	1542.6	65	No load	1.19	3.6	1.8	2.1		
JANUS	◆◆◆	Pacific	600.8	30	No load	1.12	10.0	7.7	0.0		
KAUFMANN	◆◆◆	Maximum growth	1590.6	65	0.20*	2.48†	9.0	9.0	0.0		
KEMPER BLUE CHIP A	◆	Growth/income	142.6	-25	5.75	1.38	-5.2	-5.7	1.7	123	

Includes redemption fee. * Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts. § Holding is less than 0.5% of assets.

ANNUAL TOTAL RETURNS (%)					TREND	PORTFOLIO DATA					RISK	TELEPHONE			
5 YEARS PRETAX		5 YEARS AFTER TAX		10 YEARS PRETAX	10 YEARS AFTER TAX	BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		TOLL-FREE (800)	IN-STATE
ated	10.4	7.5	12.4	9.7		Average	12	26	MG	22	Motorola(3)	High	225-5291		
	5.4	3.8				Average	9	18	MB	-4	Norwest(3)	Average	225-5291		
						Average	5	16	LB	-6	Exxon(2)		225-5291		
	8.7	6.8	12.8	10.0		Average	6	17	LB	0	General Electric(3)	Very low	225-5291		
	21.8	21.4				Low	8	33	SG	19	Viking Office Products(4)	Very high	225-5291		
ated							15	21	MG	-8	Motorola(3)		225-5291		
	14.1	11.9				Average	3	24	LG	16	United Healthcare(4)	High	422-1050	OH 419-247-2477	
	6.6	4.4				High	4	23	MB	6	Pittston Services Group(2)	Very high	422-1050	OH 419-247-2477	
	10.9	10.0				Low	7	24	LV	17	Anglo American of SA (ADR)(2)	Average	422-1050	OH 419-247-2477	
						Low	4	18	LG	-7	Kimberly-Clark De Mexico A(5)		422-1050	OH 419-247-2477	
ated	16.4	14.7	16.1	14.0		Average	6	15	SV	4	CMAC Investment(3)	Average	432-7856	WI 414-347-7777	
	8.8	6.1				Average	19	20	MB	16	FHLMC(5)	Average	421-4184	FL 813-573-8143	
	7.5	5.2				Low	4	18	LV	-2	Dow Chemical(4)	Low	433-6884		
						Very low	15	18	LV	7	Kmart(2)		258-3030		
	7.0	5.3				Low	5	14	LV	7	Ford Motor(5)	Average	346-7301	CA 213-623-7833	
ated						Average	13	35	MG	10	American Power Conversion(3)		945-3863	MN 612-376-2600	
	5.2	2.5	11.3	8.0		Very high	3	20	MB	1	Philip Morris(3)	Average	945-3863	MN 612-376-2600	
	5.9	4.6				Average	2	26	LV	5	Kamigumi(3)	High	945-3863	MN 612-376-2600	
						Average	4	23	MG	9	Minerals Technologies(3)		945-3863	MN 612-376-2600	
	8.9	6.7	15.8	12.2		High	8	22	MB	3	Motorola(2)	Average	945-3863	MN 612-376-2600	
ated	9.1	7.0				High	9	18	LB	11	Lowe's(5)	High	851-9777	FL 813-585-6565	
	9.2	6.6				High	4	18	LB	15	Lowe's(6)	High	851-9777	FL 813-585-6565	
						High	6	22	LB	2	Telefonos De Chile (ADR)(3)		851-9777	FL 813-585-6565	
	8.7	6.6				Average	7	19	LG	8	Lowe's(6)	High	851-9777	FL 813-585-6565	
						High	4	19	LB	1	Royal Dutch Petroleum(6)		328-8300	MN 612-671-3733	
ated	10.9	9.7	11.9	10.1		Average	6	27	MG	15	HBO(2)	High	328-8300	MN 612-671-3733	
						Average	19	19	MV	-4	Dow Chemical(2)		328-8300	MN 612-671-3733	
	8.3	6.1	13.4	10.4		Average	3	19	MB	16	Nucor(3)	Average	328-8300	MN 612-671-3733	
						Low	13	27	MB	-2	Castorama Dubois(2)		328-8300	MN 612-671-3733	
	12.9	7.5	15.8	11.5		Average	3	26	MG	24	Coca-Cola(3)	High	328-8300	MN 612-671-3733	
ated	5.0	3.6	14.4	12.4		Average	9	34	LV	2	Telefonica De Espana (ADR)(2)	High	328-8300	MN 612-671-3733	
	11.9	9.1				Average	5	20	LB	5	Dow Chemical(3)	Average	328-8300	MN 612-671-3733	
	8.0	5.0	12.1	8.1		Average	13	16	MV	-3	Arco Chemical(1)	Low	328-8300	MN 612-671-3733	
	13.1	11.0	17.3	14.1		Average	12	22	LG	11	Motorola(3)	Average	328-8300	MN 612-671-3733	
	1.8	1.5				Average	6	39	MG	-20	American Barrick Resources(8)	Very high	328-8300	MN 612-671-3733	
ated	7.0	5.4	10.7	7.6		Average	13	18	SV	1	Mercantile Bancorp(3)	Average	328-8300	MN 612-671-3733	
	9.5	6.0	13.6	9.7		Average	17	19	LB	1	Minnesota Mining & Mfg(1)	Low	328-8300	MN 612-671-3733	
	8.4	6.7	13.9	12.7		Average	13	27	MG	13	Intel(3)	High	328-8300	MN 612-671-3733	
	8.9	6.6	13.2	10.4		Average	18	15	LV	-1	Johnson & Johnson(1)	Low	328-8300	MN 612-671-3733	
	2.4	2.3				Average	12	30	LB	2	Cemex CI B (ADR)(2)	High	328-8300	MN 612-671-3733	
ated	7.5	5.1				High	7	18	LV	-4	AT & T(4)	Low	328-8300	MN 612-671-3733	
	8.4	5.9	12.1	8.8		Low	5	17	LV	-2	Eli Lilly(1)	Very low	421-4120	CA 415-421-9360	
	5.3	3.8				Average	5	32	LG	17	Orix(1)	High	344-8332	NY 212-841-3841	
	15.6	13.0	14.1	11.5		High	16	25	MG	5	Office Depot(2)	High	525-8085	CO 303-930-6300	
						Very high	35	21	SB	-9	Insignia Financial Grp CI A(2)		525-8085	CO 303-930-6300	
ated	3.9	3.3				Average	1	21	LV	-1	Fiat(2)	High	525-8085	CO 303-930-6300	
	9.2	6.7	11.6	8.6		Average	15	17	LB	5	Telefonos De Mexico L (ADR)(3)	Average	525-8085	CO 303-930-6300	
	12.2	9.3	15.5	11.6		Average	3	17	LV	-1	El Paso Natural Gas(2)	Low	525-8085	CO 303-930-6300	
	0.6	0.1				Average	2	30	LB	-1	Fiat(1)	High	525-8085	CO 303-930-6300	
	2.6	1.3	15.0	13.2		Low	2	36	LB	5	Asahi Bank(2)	Very high	525-8085	CO 303-930-6300	
ated	18.0	15.7				Very high	25	9	MV	-6	Citicorp(6)	High	525-8085	CO 303-930-6300	
	-4.0	-4.0	1.9	1.6		High	7	31	SG	-20	Industrias Penoles CI A2(5)	Very high	525-8085	CO 303-930-6300	
	14.4	13.6	20.8	19.6		Average	8	27	SG	7	United Healthcare(4)	High	525-8085	CO 303-930-6300	
	16.7	14.4	19.9	17.2		High	11	26	MG	5	La Quinta Inns(2)	Average	525-8085	CO 303-930-6300	
	22.5	20.2	18.9	17.5		Very high	9	24	MG	12	General Instrument(3)	High	525-8085	CO 303-930-6300	
ated	6.8	4.5				Very high	6	15	MV	-12	Southern New England Telecom(3)	Low	525-8085	CO 303-930-6300	
	8.8	7.1	14.4	11.6		Low	9	18	LB	16	FNMA(2)	Low	421-4120	CA 213-486-9200	
	7.5	4.8	11.8	8.5		Average	2	20	MB	1	Fluor(3)	Average	456-5111	FL 407-393-8900	
	9.4	8.5				Low	9	23	LV	21	Swire Pacific CI A(3)	High	456-5111	FL 407-393-8900	
	10.7	9.3	15.1	12.1		High	42	20	LG	6	General Motors(3)	Low	525-8983		
ated						Very high	35	19	LB	0	Mannesman (ADR)(4)		525-8983		
						Very high	17	28	SG	12	Exide(10)		525-8983		
						High	4	21	LG	5	Lowe's(4)		525-8983		
						Very high	46	21	MG	6	Analog Devices(6)		525-8983		
	10.9	10.4				High	13	22	LG	9	Merrill Lynch(5)	High	525-8983		
ated	12.7	10.9				High	13	23	SG	15	Wisconsin Central Transport(4)	Low	525-8983		
						High	16	28	LG	5	Mannesmann (Germany)(7)		525-8983		
	-0.5	-2.1	15.6	11.2		Average	2	50	MB	4	Nichiei(5)	Very high	535-2726	MA 617-439-4640	
	19.3	19.0				Average	3	25	SG	22	Microchip(3)	High	237-0132	NY 212-922-0123	
	7.5	6.3				Very high	3	23	LG	1	General Electric(3)	Average	621-1048	IL 312-781-1121	

DATA: MORNINGSTAR INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1994 RETURNS (%)				RANK OBJ
			ASSETS \$MIL	% CHG 1993-4	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE- TAX	AFTER- TAX	YIELD		
KEMPER GROWTH A	↓	Growth	1531.6	-8	5.75	1.09	-5.9	-6.3	0.0	191	
KEMPER INTERNATIONAL A	↓ ↓	Foreign	353.6	8	5.75	1.40	-4.0	-5.7	0.0	3	
KEMPER RETIREMENT I		Balanced	99.4	-18	5.00†	0.91	-6.3	-9.1	3.9	5	
KEMPER RETIREMENT II		Balanced	163.8	-19	5.00†	0.90	-6.8	-9.5	4.8	5	
KEMPER RETIREMENT III		Balanced	116.9	-19	5.00†	0.95	-7.3	-9.4	4.5	5	
KEMPER RETIREMENT IV		Balanced	141.5	-18	5.00	0.97	-8.2	-9.3	4.3	5	
KEMPER SMALL CAP EQUITY A	AVG	Small company	476.8	-2	5.75	1.37	-3.3	-4.9	0.0	6	
KEMPER TECHNOLOGY A	AVG	Technology	662.0	6	5.75	0.83	11.2	7.1	0.0		
KEMPER TOTAL RETURN A	AVG	Balanced	1640.4	12	5.75	1.05	-9.2	-9.9	2.6		
KEYSTONE AMER. GLOBAL OPPORT. B		World	135.9	256	3.00**	2.23†	1.9	1.9	0.0	1	
KEYSTONE AMER. HARTWELL EM GR A	↓ ↓	Small company	121.4	-31	5.75	1.94†	-1.0	-1.2	0.0	4	
KEYSTONE AMER. OMEGA A	AVG	Maximum growth	98.9	15	5.75	1.46†	-5.7	-6.7	0.0	2	
KEYSTONE CUSTODIAN K-1	AVG	Balanced	1294.8	-14	4.00**	1.71†	-4.7	-6.1	4.0	4	
KEYSTONE CUSTODIAN K-2	AVG	Growth	414.5	8	4.00**	1.80†	-3.0	-6.1	0.0	155	
KEYSTONE CUSTODIAN S-1	↓	Growth/income	188.9	-16	4.00**	2.07†	-5.9	-7.8	1.8	128	
KEYSTONE CUSTODIAN S-3	↓	Growth	231.1	-17	4.00**	1.35†	-4.7	-7.2	0.7	184	
KEYSTONE CUSTODIAN S-4	↓	Maximum growth	1171.0	14	4.00**	1.73†	0.2	-2.0	0.0	1	
KEYSTONE FUND OF THE AMERICAS B		World	141.9	644	3.00**	2.60†	-9.3	-10.0	2.3	4	
KEYSTONE INTERNATIONAL	↓ ↓ ↓	Foreign	142.9	17	4.00**	2.39†	-6.2	-9.1	0.9	4	
KEYSTONE PRECIOUS METALS HLDG.	↓ ↓ ↓	Precious metals	199.5	7	4.00**	2.25†	-13.3	-13.5	0.5	1	
KIDDER PEABODY GLOBAL EQUITY A		World	169.6	-1	5.75	1.57†	-2.3	-4.5	0.0	2	
LANDMARK BALANCED	↓ ↓	Balanced	227.4	-14	4.75	1.02†	-2.1	-3.0	2.9	2	
LANDMARK EQUITY		Growth	184.0	-8	4.75	1.05†	-0.4	-1.6	1.2	102	
LEGG MASON SPECIAL INVESTMENT	↓	Small company	605.7	19	No load	1.93†	-13.1	-13.4	0.0	8	
LEGG MASON TOTAL RETURN	↓	Growth/income	193.3	10	No load	1.93†	-7.1	-9.0	2.3	130	
LEGG MASON VALUE	↓	Growth	967.3	6	No load	1.82†	1.4	1.2	0.3	60	
LEXINGTON CORPORATE LEADERS	AVG	Growth/income	154.6	8	No load	0.62	-0.8	-5.6	3.7	80	
LEXINGTON GLOBAL	↓ ↓	World	72.8	-16	No load	1.60	1.8	-3.5	0.0	1	
LEXINGTON GOLDFUND	↓ ↓ ↓	Precious metals	151.2	14	No load	1.60†	-7.3	-7.4	0.4	0	
LEXINGTON GROWTH & INCOME	↓	Growth/income	125.0	-6	No load	1.30†	-3.1	-5.4	1.1	103	
LEXINGTON STRATEGIC INVESTMENTS	↓ ↓ ↓	Precious metals	96.0	45	5.75	1.76†	11.3	10.9	1.2		
LEXINGTON WORLDWIDE EMERGING	↓	Foreign	332.2	195	No load	1.71	-13.8	-14.9	0.0	6	
LIBERTY EQUITY-INCOME A	↓	Equity-income	100.0	67	5.50	1.03†	-3.8	-5.0	4.1	2	
LIBERTY FINANCIAL UTILITIES		Utilities	248.3	-17	4.50	1.09†	-6.9	-8.5	5.3		
LIBERTY UTILITY A	↓	Utilities	737.8	-19	5.50	1.10	-8.0	-10.7	5.2	1	
LINDNER	↓	Growth	1503.0	2	2.00*	0.65	-0.7	-3.4	1.5	108	
LINDNER DIVIDEND	↓ ↓ ↓	Income	1605.2	17	2.00*	0.64	-3.3	-6.1	7.7		
LONGLEAF PARTNERS (z)	↓ ↓ ↓	Growth	753.5	90	No load	1.21	9.0	6.8	0.9	10	
LONGLEAF PARTNERS SMALL-CAP (aa)	↓ ↓	Small company	99.6	17	No load	1.38	3.7	2.3	0.0	1	
LOOMIS SAYLES INTL. EQUITY		Foreign	71.6	27	No load	1.50	-1.8	-4.1	1.1	3	
LOOMIS SAYLES SMALL CAP		Small company	74.1	9	No load	1.29	-8.3	-8.5	0.0	8	
LORD ABBETT DEVELOPING GROWTH	↓	Small company	130.3	-2	5.75	1.34†	6.2	3.9	0.0	1	
LORD ABBETT GLOBAL EQUITY	↓ ↓	World	84.2	30	5.75	1.68†	-0.1	-2.1	0.8	1	
LORD ABBETT VALUE APPRECIATION	AVG	Growth	186.4	-4	5.75	1.22†	-3.2	-5.5	1.3	161	
MAINSTAY CAPITAL APPRECIATION B	↓ ↓	Growth	501.1	46	5.00**	1.80†	-1.5	-1.7	0.0	129	
MAINSTAY TOTAL RETURN B	↓	Balanced	648.6	17	5.00**	1.70†	-2.4	-3.1	2.4	3	
MAINSTAY VALUE B	↓ ↓	Growth/income	472.0	52	5.00**	1.90†	-0.2	-1.5	0.6	69	
MANAGERS CAPITAL APPRECIATION	↓	Growth	87.6	28	No load	1.27	-1.5	-3.3	0.5	128	
MANAGERS INTERNATIONAL EQUITY	↓	Foreign	88.4	61	No load	1.45	2.0	1.8	0.2	1	
MANAGERS SPECIAL EQUITY	AVG	Small company	112.0	19	No load	1.62	-2.0	-3.0	0.0	5	
MANNING & NAPIER SMALL CAP		Small company	100.7	NM	No load	1.13	11.2	8.9	2.8		
MARINER TOTAL RETURN EQUITY	AVG	Growth/income	71.3	-8	5.00	0.71†	-3.0	-4.3	2.4	101	
MARKETWATCH EQUITY (bb)		Growth/income	103.2	-4	4.50	1.34†	-1.1	-1.6	1.8	82	
MARQUIS GROWTH & INCOME A		Balanced	67.9	NM	3.50	0.85	-1.8	-2.9	3.6	2	
MARSHALL STOCK		Growth/income	220.6	-19	No load	0.99	-5.8	-6.0	0.7	127	
MARSHALL VALUE EQUITY		Growth/income	211.1	NM	No load	1.00	2.1	1.3	1.5	25	
MASSACHUSETTS INVESTORS A	AVG	Growth/income	1535.2	-6	5.75	0.69†	-1.0	-4.3	2.2	81	
MASSACHUSETTS INV. GROWTH A	↓ ↓	Growth	965.9	-15	5.75	0.71†	-6.7	-9.4	0.0	196	
MATHERS	AVG	Growth	293.3	-33	No load	0.89	-5.9	-7.2	5.0	190	
MENTOR GROWTH	AVG	Growth	189.5	9	5.00**	1.97†	-4.5	-6.5	0.0	183	
MENTOR STRATEGY		Asset allocation	176.4	70	5.00**	2.04†	-3.4	-3.4	0.0	2	
MERGER	↓ ↓ ↓	Growth	171.2	528	No load	1.76†	7.1	5.6	0.0	15	
MERIDIAN	↓ ↓ ↓	Small company	256.6	60	No load	1.22	0.6	-0.4	0.7	2	
MERRILL LYNCH BALANCED INV. & RET. B	AVG	Balanced	324.2	-60	4.00**	1.81†	-7.4	-10.0	1.5	5	
MERRILL LYNCH BASIC VALUE B	AVG	Growth/income	1797.2	16	4.00**	1.55†	0.9	-0.7	2.0	46	
MERRILL LYNCH CAPITAL B	↓	Growth/income	3263.6	9	4.00**	1.55†	-0.1	-2.5	3.2	67	
MERRILL LYNCH DIVERS B		Pacific	950.7	40	4.00**	2.35†	-17.0	-17.7	0.8	1	
MERRILL LYNCH EUROFUND B	↓ ↓	Europe	991.0	26	4.00**	1.93†	3.2	0.0	0.0		
MERRILL LYNCH FD. FOR TOMORROW B	↓ ↓ ↓	Growth	139.4	-65	4.00**	1.94†	-8.5	-10.2	1.7	222	
MERRILL LYNCH GLOBAL ALLOC. B	↓ ↓ ↓	Asset allocation	6266.1	38	4.00**	1.86†	-2.9	-4.3	2.5	2	

Includes redemption fee. * Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts. § Holding is less than 0.5% of assets.
(z) Formerly Southwestern Asset Mgmt Value. (aa) Formerly Southeastern Asset Mgmt Small-Cap. (bb) Formerly CFB MarketWatch Equity.

Equity Funds

ANNUAL TOTAL RETURNS (%)					TREND	PORTFOLIO DATA						RISK	TELEPHONE			
5 YEARS		10 YEARS		BW 10-YEAR ANALYSIS		TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		TOLL-FREE (800)	IN-STATE		
PRETAX	AFTERTAX	PRETAX	AFTERTAX													
10.3	9.0	13.7	10.7		High	2	23	LG	6	Nucor(2)	High	621-1048	IL	312-781-1121		
4.6	2.9	15.3	12.6		High	8	33	LB	4	STET(3)	High	621-1048	IL	312-781-1121		
					Average	3	24	MG	2	Nucor(1)		621-1048	IL	312-781-1121		
					Average	2	24	MG	0	Nucor(1)		621-1048	IL	312-781-1121		
					Average	3	24	MG	-2	Nucor(1)		621-1048	IL	312-781-1121		
					Average	4	22	MG	-14	Promus(1)		621-1048	IL	312-781-1121		
12.6	10.3	13.7	10.7		Average	13	25	SG	23	Viking Office Products(4)	High	621-1048	IL	312-781-1121		
12.2	8.8	13.4	9.7		High	10	25	MG	23	Compaq Computer(4)	High	621-1048	IL	312-781-1121		
8.7	6.6	11.3	8.9		Very high	8	20	MB	0	Promus(2)	Low	621-1048	IL	312-781-1121		
						6	26	SG	4	Goldman Sachs Group(6)		343-2898	MA	617-338-3400		
13.1	12.0	17.0	15.0		High	4	39	SG	27	General Datascomm Industries(10)	Very high	343-2898	MA	617-338-3400		
12.0	8.5	15.7	12.3		High	19	23	MG	5	EMC(3)	High	343-2898	MA	617-338-3400		
5.8	3.9	10.4	7.5		High	3	18	LB	6	General Electric(3)	Low	343-2898	MA	617-338-3400		
9.4	6.5	13.0	9.9		Average	1	24	MG	11	EMC(4)	Average	343-2898	MA	617-338-3400		
4.9	2.5	10.3	7.8		Average	5	20	LB	7	General Electric(4)	Average	343-2898	MA	617-338-3400		
7.2	4.7	11.2	8.2		Average	11	21	MG	12	Intel(2)	High	343-2898	MA	617-338-3400		
17.5	14.9	14.8	12.1		Average	5	26	MG	27	EMC(4)	Very high	343-2898	MA	617-338-3400		
						4	27	MG	-12	Telebras(3)		343-2898				
1.7	0.5	11.6	9.6		Average	8	32	LB	2	HSBC Holdings New(8)	High	343-2898	MA	617-338-3400		
3.8	3.5	8.6	7.7		Average	3	32	SG	5	Franco-Nevada Mining(6)	Very high	343-2898	MA	617-338-3400		
					Average	3	24	LB	9	Astra CI B Free(3)		854-2505	NY	212-656-1737		
					High	2	20	LB	-3	General Electric(2)	Low		MA	212-559-7117		
					Low	21	20	LB	3	Home Depot(3)			MA	212-559-7117		
11.8	10.3				Very low	8	22	SB	8	Caesars World(4)	Average	822-5544	MD	410-539-0000		
7.2	5.9				Average	8	13	MV	-3	Grupo Finan Serfin (ADR)(4)	Average	822-5544	MD	410-539-0000		
7.1	6.6	11.1	9.6		Very low	3	13	LV	32	FNMA(6)	Average	822-5544	MD	410-539-0000		
7.9	3.9	14.9	10.0			1	16	LV	35	Mobil(9)	Low	526-0057	NJ	201-845-7300		
4.5	2.5				High	5	30	MB	-3	Telefonos De Mexico L (ADR)(2)	High	526-0057	NJ	201-845-7300		
0.5	0.3	8.9	8.5		Low	3	34	MG	0	Newcrest Mining(5)	Very high	526-0057	NJ	201-845-7300		
6.7	4.1	10.7	7.2		Average	9	21	MB	-1	Ingersoll-Rand(2)	Average	526-0057	NJ	201-845-7300		
-5.5	-5.9	-2.5	-4.0		Low	5	14		-80	Western Areas Gold Mine ADR(12)	Very high	526-0057	NJ	201-845-7300		
9.3	7.0	12.9	10.1		Average	13	26	MG	-6	Sociedad Anonima (ADR)(3)	High	526-0057	NJ	201-845-7300		
9.5	7.3				Average	4	17	LV	-6	Sprint(2)	Low	245-5051	PA	412-288-1900		
					Average	8	15	LV	-7	Powergen (ADR)(3)		872-5426	MA	617-722-6000		
8.2	5.8				Low	5	16	MV	-6	Sonat(3)	Very low	245-5051	PA	412-288-1900		
8.0	6.0	12.3	8.8		Average	7	22	SB	9	Minorco (ADR)(2)	Low		MO	314-727-5305		
9.9	7.0	11.7	8.0		Average	5	21	MB	-9	Telefonos De Mexico L (ADR)(2)	Very low		MO	314-727-5305		
13.3	11.3				Low	5	15	MB	8	Knight-Ridder(6)	Low	445-9469	TN	901-761-2474		
3.2	2.4				Very low	6	22	SV	8	Helene Curtis Industries(7)	Average	445-9469	TN	901-761-2474		
					High	1	16	MV	1	Tessenderlo Chemie(1)		633-3330	MA	617-482-2450		
					Average	7	21	SB	-2	Int'l Cabletel(2)		633-3330	MA	617-482-2450		
11.1	9.6	8.8	7.3		Low	9	24	SG	53	Applied Materials(7)	High	874-3733	NY	212-848-1800		
4.5	3.4				Very high	12	26	LV	2	Orix(1)	Average	874-3733	NY	212-848-1800		
8.8	6.8	12.3	9.2		Low	17	17	MV	22	Kerr-McGee(3)	Average	874-3733	NY	212-848-1800		
16.9	15.3				Low	8	19	MB	12	3Com(3)	High	522-4202				
9.9	8.8				Very high	5	19	MB	5	3Com(2)	Low	522-4202				
12.4	10.5				Average	7	16	MV	-1	Occidental Petroleum(2)	Low	522-4202				
11.7	8.7	14.7	10.4		High	20	21	MB	3	Motorola(2)	Average	835-3879	CT	203-857-5321		
9.4	8.6				Low	13	33	LB	13	Sap(2)	Average	835-3879	CT	203-857-5321		
11.0	8.6	15.1	12.3		Average	12	21	SB	11	Airborne Freight(2)	High	835-3879	CT	203-857-5321		
					Very low	NA	NA		13	NA		466-3863				
8.0	5.8				Very low	1	22	LB	-2	Exxon(2)	Average	634-2536	CO	305-421-8878		
						12	16	MB	-1	Mattel(3)		232-9091				
					Very low	17	14	MV	-6	Textron(1)		462-9511				
					Average	7	18	LB	-1	Shaw Industries(4)		236-8560	PA	414-287-8500		
						8	NA		-4	NA		236-8560	PA	414-287-8500		
8.3	4.2	13.4	9.1		Average	5	17	LB	12	General Electric(2)	Low	637-2929	MA	617-954-5000		
9.5	6.8	12.8	9.0		Average	4	24	LG	23	Home Depot(6)	High	637-2929	MA	617-954-5000		
3.7	2.1	10.8	6.8		High	4	16	SV	-12	Nature's Bounty(6)	Very low	962-3863	IL	708-295-7400		
11.2	9.4				Average	14	21	SB	19	Swift Transportation(2)	High	825-5353	VA	804-649-2311		
						21	20	MB	-1	First USA(1)		825-5353	VA	804-649-2311		
9.4	7.5				Very high	7	19	SV	0	Colonial Group(4)	Very low	343-8959	NY	914-741-5600		
16.6	15.0	15.0	12.9		Average	29	26	SG	5	Service International(3)	Average	446-6662	CA	415-461-6237		
5.6	3.1				Average	8	19	MB	12	Singer(3)	Low	637-3863	NJ	609-282-2800		
7.6	6.0				Low	19	16	LV	13	Sears Roebuck(4)	Average	637-3863	NJ	609-282-2800		
7.6	5.6				Average	2	16	LV	0	NationsBank(2)	Low	637-3863	NJ	609-282-2800		
						8	25	MG	19	San Miguel CI B(2)		637-3863	NJ	609-282-2800		
7.0	6.1				High	5	22	LV	2	BBC Brown Boveri (BR)(3)	High	637-3863	NJ	609-282-2800		
5.0	2.4	10.7	8.1		Average	4	19	LB	20	Chrysler(5)	Average	637-3863	NJ	609-282-2800		
10.7	8.2				Average	3	20	LV	-4	Chemical Banking(1)	Very low	637-3863	NJ	609-282-2800		

DATA: MORNINGSTAR INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1994 RETURNS (%)				RANK OBJ
			ASSETS \$MIL	% CHG 1993-4	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE- TAX	AFTER- TAX	YIELD		
MERRILL LYNCH GLBL. RESOURCES B (cc)	♦♦	Natural resources	223.5	14	4.00**	1.95†	0.2	0.1	0.2		
MERRILL LYNCH GLOBAL UTILITY B		Utilities	459.2	-23	4.00**	1.59†	-10.6	-11.5	3.2		
MERRILL LYNCH GROWTH INV. & RET. B	AVG	Growth	1321.9	27	4.00**	1.80†	0.7	0.2	0.0	7	
MERRILL LYNCH INTL. EQUITY B		Foreign	1039.4	161	4.00**	2.07†	-0.6	-2.1	0.4		
MERRILL LYNCH LATIN AMERICA B		Foreign	937.6	208	6.00***	2.39†	-15.9	-16.7	0.0		
MERRILL LYNCH PACIFIC B	♦♦	Pacific	909.3	98	4.00**	1.87†	1.8	1.1	0.2		
MERRILL LYNCH PHOENIX B	AVG	Growth	347.8	36	4.00**	2.24†	-7.4	-10.4	0.2	20	
MERRILL LYNCH SPECIAL VALUE B	♦	Small company	169.4	101	4.00**	2.19†	2.8	0.2	0.0		
MERRILL LYNCH STRATEGIC DIV B	♦	Equity-income	138.3	-36	4.00**	1.88†	-0.2	-4.9	2.6		
MERRILL LYNCH TECHNOLOGY B		Technology	572.0	322	4.00**	2.36†	25.5	22.9	1.2		
METLIFE-STATE ST RES. CAP. APPR. A (dd)	♦	Maximum growth	254.1	14	4.50	1.50†	-2.5	-3.7	0.0		
METLIFE-STATE ST RES MGD. ASSET A (ee)	♦	Asset allocation	179.7	41	4.50	1.25†	-5.9	-6.9	2.0		
MFS CAPITAL GROWTH B	AVG	Growth	394.9	-13	4.00**	2.19†	-0.9	-2.3	0.4	11	
MFS EMERGING GROWTH B	♦♦♦	Small company	801.4	18	4.00**†	2.23†	4.0	3.6	0.0		
MFS GROWTH OPPORTUNITIES A	♦♦	Growth	588.8	-17	5.75	0.85†	-4.2	-6.4	0.3	179	
MFS MANAGED SECTORS B	♦♦	Growth	197.5	-17	4.00**	2.26†	-3.5	-5.6	0.0	166	
MFS RESEARCH A	♦	Growth	321.4	8	5.75	0.91†	0.0	-2.7	0.1	9	
MFS TOTAL RETURN A	♦	Balanced	1825.1	5	4.75	0.79†	-2.7	-3.9	4.3		
MFS VALUE A	AVG	Growth	142.8	3	5.75	1.34†	-2.5	-4.5	0.0	148	
MFS WORLD EQUITY B	♦	World	163.7	4	4.00**	2.61†	-3.7	-6.3	0.0		
MFS WORLD GROWTH B		World	229.7	153	4.00**	2.57†	2.0	1.8	0.0		
MFS WORLD TOTAL RETURN A		World	95.4	26	4.75	1.78†	-3.1	-4.6	1.9		
MONETTA	♦	Small company	364.9	-30	No load†	1.36	-6.2	-6.3	0.0		
MONTGOMERY EMERGING MARKETS		Foreign	878.0	44	No load	1.85	-7.7	-9.1	0.0		
MONTGOMERY GLOBAL COMMUNICATIONS		Utilities	216.4	-2	No load	1.94	-13.4	-13.5	0.0		
MONTGOMERY GROWTH		Growth	592.7	NM	No load	1.49	20.9	20.6	0.4		
MONTGOMERY SMALL CAP		Small company	202.5	-22	No load†	1.35	-10.0	-11.5	0.0		
MORGAN STANLEY ASIAN GROWTH A		Pacific	158.5	22	4.75	1.90†	-14.2	-15.0	0.0		
MUTUAL BEACON	♦♦♦	Growth/income	2056.4	94	No load	0.72	5.6	3.9	3.3		
MUTUAL DISCOVERY		Small company	725.8	33	No load†	0.99	3.6	1.4	5.1		
MUTUAL QUALIFIED	♦♦♦	Growth/income	1788.8	16	No load	0.76	5.7	3.7	2.8		
MUTUAL SHARES	♦♦	Growth/income	3745.3	6	No load	0.73	4.5	2.4	3.0		
NATIONS EQUITY-INDEX TR. A		Growth	123.1	NM	No load	0.35	1.0	-0.2	2.6		
NATIONWIDE	AVG	Growth/income	636.8	-13	4.50	0.63	0.6	-2.2	1.9	50	
NATIONWIDE GROWTH	AVG	Growth	439.8	2	4.50	0.68	1.5	0.3	1.7	57	
NEUBERGER & BERMAN FOCUS (ff)	♦	Growth	603.1	2	No load	0.85	0.9	-1.2	0.9	70	
NEUBERGER & BERMAN GENESIS	AVG	Small company	108.0	-13	No load	1.36	-1.8	-2.9	0.0	5	
NEUBERGER & BERMAN GUARDIAN	♦♦	Growth/income	2423.8	21	No load	0.80	1.4	0.4	2.2	30	
NEUBERGER & BERMAN MANHATTAN	♦	Growth	462.2	-12	No load	0.96	-3.6	-5.4	0.1	169	
NEUBERGER & BERMAN PARTNERS	♦	Growth	1245.2	10	No load	0.81	-1.9	-4.2	0.5	136	
NEW ECONOMY	AVG	Growth	2594.4	23	5.75	0.85†	-8.1	-9.7	1.2	217	
NEW ENGLAND BALANCED A (gg)	AVG	Balanced	197.5	25	5.75	1.43†	-2.6	-4.0	2.9		
NEW ENGLAND CAPITAL GROWTH A (hh)		Growth	95.7	-3	5.75	1.66†	-1.6	-1.6	0.0	131	
NEW ENGLAND GROWTH A (ii)	♦	Growth	989.0	-17	6.50†	1.18†	-7.1	-9.3	1.2	203	
NEW ENGLAND GROWTH OPPORT A (jj)	AVG	Growth/income	103.5	-4	5.75	1.33†	1.0	0.1	1.7	41	
NEW ENGLAND INTL EQUITY A (kk)		Foreign	140.6	102	5.75	1.75†	8.1	7.0	0.0		
NEW ENGLAND VALUE A (ll)	♦♦	Growth/income	195.4	3	5.75	1.38†	-1.4	-3.2	1.0	87	
NEW PERSPECTIVE	♦	World	6540.2	29	5.75	0.84†	3.0	0.9	1.5		
NEW USA MUTUAL		Growth	183.0	-34	5.00	2.11†	-3.6	-3.6	0.0	166	
NEW YORK VENTURE A	♦	Growth	1090.5	16	4.75	0.87†	3.2	0.4	2.0	39	
NEWPORT TIGER	♦	Pacific	455.9	15	5.00	1.56	-12.0	-12.3	0.3	1	
NICHOLAS	AVG	Growth	2820.2	-11	No load	0.80	-2.8	-5.0	1.4	153	
NICHOLAS II	AVG	Small company	603.9	-14	No load	0.67	1.0	-1.2	0.8	2	
NICHOLAS LIMITED EDITION	♦♦	Small company	142.6	-21	No load†	0.88	-3.0	-4.6	0.6	5	
NICHOLAS-APPLEGATE CORE GR. B		Growth	134.8	5	1.00**	2.17†	-11.5	-11.5	0.0	232	
NICHOLAS-APPLEGATE EMERG. GR. B		Small company	143.8	NM	2.00***†	2.34†	-4.7	-4.7	0.0	7	
NICHOLAS-APPLEGATE GRTH. EQ. B		Maximum growth	254.5	12	5.00**	2.22†	-10.2	-10.9	0.0	3	
NICHOLAS-APPLEGATE WORLD GR. B		World	77.6	69	1.00**	2.44†	1.9	1.5	0.3		
NORTH AMERICAN ASSET ALLOC. C	♦	Asset allocation	82.2	-20	No load	1.99†	-2.8	-4.8	2.3	2	
NORTH AMERICAN GLOBAL GROWTH C		World	95.5	26	No load	2.40†	1.2	0.3	0.0	1	
NORTH AMERICAN GROWTH C	♦	Growth	69.3	-2	No load	1.99†	-2.2	-3.7	0.0	141	
NWNL NORTHSTAR INCOME & GROWTH A		Balanced	69.4	NM	4.75	1.46†	-3.6	-4.5	3.3	3	
OAKMARK		Growth	1626.9	34	No load	1.25	3.3	1.3	0.9	35	
OAKMARK INTERNATIONAL		Foreign	1079.7	-3	No load	1.32	-9.1	-11.1	0.0	5	
OBERWEIS EMERGING GROWTH	AVG	Small company	90.1	-11	No load	1.78†	-3.5	-3.5	0.0	6	
OLD WESTBURY INTERNATIONAL		Foreign	89.6	100	4.50	1.50†	-11.1	-11.3	0.8	5	
OPPENHEIMER A	AVG	Growth	246.1	10	5.75	1.16†	0.3	-2.6	0.2	81	
OPPENHEIMER ASSET ALLOCATION A	♦	Asset allocation	240.2	-12	5.75	1.14†	-1.6	-4.6	4.3	1	
OPPENHEIMER DISCOVERY A	♦	Small company	592.0	1	5.75	1.20†	-11.2	-12.3	0.0	8	
OPPENHEIMER EQUITY-INCOME A	AVG	Equity-income	1715.8	-7	5.75	0.90†	-2.8	-4.7	5.2	2	

* Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts. § Holding is less than 0.5% of assets.
(cc) Formerly Merrill Lynch Natural Resources B. (dd) Formerly MetLife-State Street Capital Appr A. (ee) Formerly MetLife-State Street Managed Assets A. (ff) Formerly Neuberger & Berman Selected Sectors. (gg) Formerly TNE Balanced A. (hh) Formerly TNE Capital Growth A. (ii) Formerly TNE Growth A. (jj) Formerly TNE Growth Opportunities A. (kk) Formerly TNE Growth Opportunities A. (ll) Formerly TNE Growth Opportunities A.

Equity Funds

ANNUAL TOTAL RETURNS (%)				TREND	PORTFOLIO DATA							RISK	TELEPHONE			
5 YEARS PRETAX		AFTERTAX		10 YEARS PRETAX	10 YEARS AFTERTAX	BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		TOLL-FREE (800)	IN-STATE	
2.7	2.0						Average	13	27	MB	-11	Weyerhaeuser(5)	Average	637-3863	NJ	609-282-2800
							Very low	4	16	LV	-3	China Light & Power(3)		637-3863	NJ	609-282-2800
12.0	10.4						Low	4	31	SG	17	Applied Materials(9)	High	637-3863	NJ	609-282-2800
rated								14	31	LV	-4	Canon(2)		637-3863	NJ	609-282-2800
							Low	9	25		-9	Grupo Carso (ADR)(4)		637-3863	NJ	609-282-2800
5.1	3.4						Very low	11	35	LB	10	Toyo Seikan Kaisha(4)	High	637-3863	NJ	609-282-2800
9.6	5.8						Average	9	18	SV	-9	ADT(3)	High	637-3863	NJ	609-282-2800
8.2	7.1						Average	25	18	SV	-1	Charter One Financial(3)	High	637-3863	NJ	609-282-2800
4.2	2.0						Low	10	18	LV	9	Sonat(4)	Low	637-3863	NJ	609-282-2800
rated							Very high	57	17	MG	2	Micron Technology(20)		637-3863	NJ	609-282-2800
14.5	13.0						High	2	25	MG	9	Hospitality Franchise System(3)	Very high	882-3302	MA	617-357-7800
7.7	5.7						High	9	24	MB	-5	United Healthcare(1)	Very low	882-3302	MA	617-357-7800
7.4	5.7						Average	2	16	LV	10	Norwest(3)	Average	637-2929	MA	617-954-5000
21.4	20.8						Average	3	26	SG	31	Oracle Systems(6)	Very high	637-2929	MA	617-954-5000
7.0	4.6	10.5	7.4				Average	6	21	MG	6	Intel(4)	Average	637-2929	MA	617-954-5000
7.4	5.7						Average	4	25	MG	5	Rogers Comm Cl B(7)	High	637-2929	MA	617-954-5000
11.0	8.3	13.8	10.2				Average	7	22	MG	12	Lin Broadcasting(2)	Average	637-2929	MA	617-954-5000
7.9	6.0	12.8	9.9				High	23	17	LV	8	Royal Dutch Petroleum(1)	Very low	637-2929	MA	617-954-5000
9.5	6.7	13.7	10.4				High	11	21	SB	4	First Interstate Bancorp(3)	Average	637-2929	MA	617-954-5000
5.2	4.2						Average	5	21	MB	8	Astra Cl B(3)	Average	637-2929	MA	617-954-5000
rated								15	33	MG	2	Fiat(2)		637-2929	MA	617-954-5000
							High	13	20	LB	0	DSM(1)		637-2929	MA	617-954-5000
11.5	10.1						Very high	16	24	MB	-6	Glenayre Technologies(3)	Average	666-3882	IL	708-462-9800
rated							Average	12	30	MG	7	Korea Electric Power(1)		572-3863	CA	415-627-2400
rated							Low	3	23	MG	-6	Tele Danmark(3)		572-3863	CA	415-627-2400
rated								23	25	MG	6	Xerox(4)		572-3863		
rated							High	4	22	SB	11	ALC Communications(6)		572-3863	CA	415-627-2400
rated							Very low	5	26	LG	2	Hutchison Whampoa(3)		282-4404		
11.5	9.6	15.4	13.1				Average	14	16	MV	6	Sunbeam-Oster(2)	Very low	553-3014	NJ	201-912-2100
rated							High	6	14	SV	3	Sears Roebuck(2)		553-3014	NJ	201-912-2100
11.6	9.3	15.1	11.9				Average	11	16	MV	16	Sunbeam-Oster(7)	Low	553-3014	NJ	201-912-2100
10.9	8.6	14.8	11.6				Average	10	17	MV	18	Sunbeam-Oster(7)	Low	553-3014	NJ	201-912-2100
rated								4	NA		-2	NA		321-7854		
7.6	5.5	14.0	10.8				Low	1	18	MG	24	Ford Motor(4)	Low	848-0920	OH	614-249-7855
8.6	7.0	13.1	10.4				Very low	14	22	LB	20	Grand Metropolitan (ADR)(4)	Average	848-0920	OH	614-249-7855
10.8	8.5	13.1	9.7				Average	1	14	LV	21	Capital Cities/ABC(3)	Average	877-9700	NY	212-476-8800
8.9	8.0						Average	2	15	SV	12	DH Technology(3)	Average	877-9700	NY	212-476-8800
12.1	10.5	14.3	11.1				Low	5	16	LV	15	Texas Instruments(2)	Average	877-9700	NY	212-476-8800
8.5	5.9	13.9	11.2				Average	0	17	MB	7	Wells Fargo(3)	High	877-9700	NY	212-476-8800
9.3	6.8	13.2	9.8				Average	4	16	MB	2	Progressive(3)	Average	877-9700	NY	212-476-8800
10.3	8.1	15.3	12.8				Low	26	24	MG	13	Tele-Communications Cl A(5)	Average	421-4120	CA	213-486-9200
7.9	6.6	10.4	7.9				Average	1	15	LB	2	Pfizer(1)	Low	225-7670	MA	617-578-1400
rated							Average	3	23	MG	6	First Bank System(3)		225-7670	MA	617-578-1400
9.7	7.3	13.2	10.4				High	1	11	LV	0	Chemical Banking(6)	High	225-7670	MA	617-578-1400
8.3	6.6	11.9	9.0				Very low	4	18	LB	27	AT&T(2)	Average	225-7670	MA	617-578-1400
rated							High	10	36	LV	4	Mitsukoshi(2)		225-7670	MA	617-578-1400
7.8	6.2	12.6	9.6				Low	3	15	LV	10	Praxair(2)	High	225-7670	MA	617-578-1400
10.3	8.8	16.0	13.3				Low	20	22	LB	17	Telefonos De Mexico L (ADR)(2)	Average	421-4120	CA	213-486-9200
rated							Very high	30	36	SG	4	Microtouch Systems(4)		222-2872		
12.9	10.4	17.4	13.6				Very low	1	17	LV	16	Sunamerica(3)	Average	279-0279	NM	505-983-4335
15.0	14.8						Very low	9	21	LG	20	Swire Pacific Cl A(4)	High	776-5455		
9.4	8.0	12.7	10.7				Low	12	17	MB	23	FNMA(3)	Average		WI	414-272-6133
9.1	7.6	13.0	11.4				Low	6	19	SB	31	Health Management Assoc Cl A(4)	Average		WI	414-272-6133
11.7	10.2						Very low	6	18	SB	31	Keane(6)	Average		WI	414-272-6133
rated								6	23	MB	-9	Compuware(3)		551-8043		
rated							Very low	1	22	SB	-3	Danka Business Systems (ADR)(2)		551-8043		
							High	3	23	MB	3	Georgia Gulf(2)		225-1852		
rated								4	25	MB	2	Empresas La Moderna (ADR)(1)		551-8043		
3.6	2.8						Very high	1	19	MV	-1	National Medical Enterprises(3)	Low	872-8037	MA	617-266-6004
							Average	4	29	LB	4	Fiat(3)		872-8037	MA	617-266-6004
6.3	5.9						Average	11	19	MV	5	National Medical Enterprises(5)	Average	872-8037	MA	617-266-6004
rated								9	15	LV	-6	General Motors(4)			CT	203-863-6215
							Low	9	18	MB	8	Philip Morris(6)		625-6275		
rated							Low	5	20	MV	-9	Banco Popular Espanol(5)		625-6275		
17.7	16.2						Average	3	26	SG	13	US Robotics(3)	Very high	323-6166	IL	708-897-7100
rated								5	19	MV	-7	Western Mining(3)		545-1074		
9.0	6.8	10.6	7.9				Average	10	20	MB	16	Intel(2)	Low	525-7048	CO	303-671-3200
7.3	5.6						Low	9	20	MB	5	Intel(1)	Very low	525-7048	CO	303-671-3200
12.3	11.2						Average	14	26	SG	8	EMC(2)	High	525-7048	CO	303-671-3200
6.6	4.5	11.9	8.9				Low	3	15	LV	4	Philip Morris(2)	Low	525-7048	CO	303-671-3200

DATA: MORNINGSTAR INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1994 RETURNS (%)			
			ASSETS \$MIL	% CHG 1993-4	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	RANK (OBJ)
OPPENHEIMER GLOBAL A	♦	World	1879.5	27	5.75	1.12†	-3.1	-6.0	0.0	2
OPPENHEIMER GLBL. EMERG. GRTH. (mm)	♦♦♦	World	169.3	-22	5.75	1.73†	-27.5	-27.5	0.0	4
OPPENHEIMER GLOBAL GRTH & INC. A	♦	World	124.1	26	5.75	1.48†	-4.7	-7.0	2.8	3
OPPENHEIMER GOLD & SPEC. MIN.	♦♦♦	Precious metals	175.5	8	5.75	1.31†	-6.0	-6.1	0.5	
OPPENHEIMER GROWTH A (nn)	AVG	Growth	678.6	-8	5.75	1.07†	2.4	-0.7	0.9	49
OPPENHEIMER MAIN ST. INC. & GRTH. A	♦♦♦	Growth/income	1187.9	997	5.75	1.23†	-1.5	-2.2	2.1	88
OPPENHEIMER TARGET A	♦	Maximum growth	303.6	-18	5.75	1.07†	0.5	-3.0	0.8	
OPPENHEIMER TIME	♦♦	Growth	313.9	-21	5.75	0.94†	-12.8	-15.2	0.0	234
OPPENHEIMER TOTAL RETURN A	AVG	Growth/income	1230.8	6	5.75	0.93†	-7.9	-8.6	2.7	132
OPPENHEIMER VALUE STOCK A	AVG	Growth/income	89.9	3	5.75	1.41†	3.3	1.8	2.2	14
PACIFIC EUROPEAN GROWTH		Foreign	165.7	12	4.00	1.81†	-3.6	-5.5	0.0	3
PACIFIC HORIZON AGGRESSIVE GRTH.	♦♦	Maximum growth	125.5	-27	4.50	1.48	-11.5	-15.8	0.0	3
PACIFICA BALANCED		Balanced	99.1	-13	4.50	1.09†	-3.8	-6.2	4.2	3
PACIFICA EQUITY VALUE		Growth	157.4	1	4.50	0.99†	-1.7	-3.9	2.0	135
PAINWEBBER ASSET ALLOCATION A		Asset allocation	173.5	-16	4.50	1.19†	-9.9	-13.4	2.2	3
PAINWEBBER ATLAS GLOBAL A	♦♦♦	World	189.8	2	4.50	1.39†	-12.8	-13.5	0.0	4
PAINWEBBER DIVIDEND GROWTH B	♦	Growth/income	251.0	-38	5.00**	1.97†	-6.6	-8.3	0.4	129
PAINWEBBER EUROPE GROWTH A	♦	Europe	73.4	-21	4.50	1.64†	-8.2	-8.2	0.0	1
PAINWEBBER GROWTH A	♦	Growth	127.5	-9	4.50	1.21†	-10.9	-10.9	0.0	229
PARAGON GULF SOUTH GROWTH		Growth	77.5	3	4.50	0.97	-7.7	-8.4	0.0	211
PARAGON VALUE EQUITY-INCOME	♦	Growth/income	103.4	1	4.50	0.93	-2.9	-6.0	2.6	100
PARAGON VALUE GROWTH	♦	Growth	196.6	15	4.50	0.94	-3.6	-6.3	1.5	167
PARKSTONE HIGH-INC. EQUITY INV. A		Equity-income	71.3	7	4.50	1.40†	-8.3	-9.1	2.8	3
PARNASSUS	♦♦♦	Growth	151.8	60	3.50	1.26	12.0	9.5	1.3	6
PASADENA GROWTH A	♦♦	Growth	391.8	-27	5.50	1.60†	-3.8	-3.8	0.0	175
PASADENA FIFTY FIFTY A		Growth	100.6	-25	5.50	1.90†	1.1	1.1	0.0	65
PAX WORLD	♦	Balanced	388.3	-16	No load	0.99†	2.6	1.5	3.7	
PBHG EMERGING GROWTH (oo)		Small company	142.7	339	2.00*	1.41	23.8	23.7	0.0	
PBHG GROWTH	♦♦♦	Small company	657.9	745	2.00*	1.40	4.8	4.7	0.0	1
PELICAN	♦	Growth/income	105.8	10	No load	1.10	3.1	0.8	3.1	15
PENN SQUARE MUTUAL	AVG	Growth/income	241.8	-4	4.75	0.99†	0.2	-2.0	2.1	57
PENNSYLVANIA MUTUAL	♦	Small company	785.8	-24	1.00*	0.97	-0.7	-3.6	1.4	4
PEOPLES INDEX	AVG	Growth/income	233.8	-18	1.00*	0.39	0.7	-2.5	2.7	49
PEOPLES S&P MIDCAP INDEX		Growth	73.4	8	1.00*	0.09	-4.0	-5.7	1.7	177
PERMANENT PORTFOLIO	AVG	Asset allocation	72.0	-7	No load	1.25†	-2.9	-3.3	1.3	2
PHILADELPHIA	♦♦	Growth/income	80.5	-15	No load	1.70†	-8.6	-9.1	1.5	135
PHOENIX BALANCED A	♦	Balanced	2502.5	-19	4.75	0.98†	-4.6	-5.5	3.2	4
PHOENIX CAPITAL APPRECIATION A	♦♦♦	Growth	419.8	-1	4.75	1.36†	-3.8	-5.4	0.6	174
PHOENIX EQUITY OPPORTUNITIES A	♦	Growth	173.9	-21	4.75	1.26†	-5.1	-7.1	1.2	187
PHOENIX GROWTH A	AVG	Growth	2036.6	-18	4.75	1.18†	-1.6	-3.1	1.4	130
PHOENIX INCOME & GROWTH A	♦	Balanced	499.9	-14	4.75	1.23†	-6.3	-9.2	5.5	4
PHOENIX INTERNATIONAL A	♦♦	Foreign	168.0	84	4.75	1.56†	-0.2	-2.2	0.0	2
PHOENIX TOTAL RETURN A	♦♦	Asset allocation	337.0	196	4.75	1.17†	-2.3	-2.9	2.1	1
PHOENIX U.S. STOCK A (pp)	♦	Growth	132.5	-7	4.75	1.31†	-3.9	-6.3	1.7	176
PHOENIX WORLDWIDE OPPORTUN. A	♦♦	World	137.9	39	4.75	1.50†	0.0	-4.7	0.3	1
PIC ENDEAVOR GROWTH		Growth	70.8	-1	No load	1.00	-2.2	-2.2	0.2	140
PIERPONT CAPITAL APPRECIATION	♦♦	Small company	177.3	-26	No load	0.90	-5.9	-8.1	1.0	7
PIERPONT EQUITY	♦	Growth/income	235.1	-1	No load	0.90	-0.6	-4.4	1.6	78
PIERPONT INTERNATIONAL EQUITY		Foreign	200.2	23	No load	1.38	5.7	4.3	0.0	
PILGRIM MAGNACAP	AVG	Growth/income	198.1	-2	5.00	1.53†	4.1	2.2	1.2	11
PIMCO ADV EQUITY-INCOME C (qq)	AVG	Equity-income	168.7	48	1.00**	2.00†	-5.1	-5.6	2.0	3
PIMCO ADV GROWTH C (rr)	AVG	Growth	1062.7	1	1.00**	1.90†	-0.7	-2.3	0.0	107
PIMCO ADV INTERNATIONAL C (ss)	♦♦♦	Foreign	274.6	50	1.00**	2.20†	-8.2	-8.7	0.0	5
PIMCO ADV OPPORTUNITY C (tt)	♦♦♦	Maximum growth	539.7	-8	1.00**†	1.90†	-4.7	-5.6	0.0	2
PIMCO ADV TARGET C (uu)		Growth	557.2	60	1.00**	2.00†	3.1	2.7	0.0	40
PIONEER	♦	Growth/income	2010.9	-2	5.75	0.95†	-0.6	-2.8	2.2	77
PIONEER CAPITAL GROWTH A		Growth	437.8	115	5.75	1.29†	14.8	13.0	0.0	4
PIONEER EQUITY-INCOME A		Equity-income	175.0	17	5.75	1.25†	-1.3	-3.0	3.5	1
PIONEER GROWTH	♦♦	Small company	132.6	-2	5.75	1.38†	-2.6	-10.0	0.0	5
PIONEER II	♦	Growth/income	4335.1	-5	5.75	0.90†	-1.7	-4.8	1.5	89
PIONEER INCOME	♦	Income	259.9	-12	4.50	1.07†	-4.3	-6.4	7.4	
PIONEER INTERNATIONAL GROWTH A		Foreign	281.4	122	5.75	1.98†	-5.4	-6.8	0.0	4
PIONEER THREE	AVG	Small company	970.9	-9	5.75	0.87†	-5.7	-7.7	1.2	7
PIPER JAFFRAY EMERGING GROWTH		Small company	209.2	1	4.00	1.24†	-4.9	-4.9	0.0	7
PIPER JAFFRAY EQUITY STRATEGY (vv)	AVG	Maximum growth	70.1	-19	4.00	1.32†	-2.5	-2.6	0.5	1
PIPER JAFFRAY VALUE	♦	Growth	176.1	-28	4.00	1.23†	-3.5	-3.7	0.4	165
PORTICO BALANCED RET.		Balanced	103.4	19	No load	0.74	-4.3	-4.9	2.1	4
PORTICO EQUITY INDEX RET.	AVG	Growth/income	106.5	39	No load	0.50	1.0	0.2	2.4	40
PORTICO GROWTH & INCOME RET.	AVG	Growth/income	162.3	-2	No load	0.89	0.1	-1.2	1.9	60
PORTICO MIDCORE GROWTH RET.		Growth	112.6	17	No load	0.86	-5.3	-5.4	0.3	188

Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts. § Holding is less than 0.5% of assets.
 (mm) Formerly Oppenheimer Global Bio-Tech. (nn) Formerly Oppenheimer Special A. (oo) Formerly Pilgrim Baxter Emerging Growth. (pp) Formerly Phoenix Stock. (qq) Formerly
 Equity Income B. (rr) Formerly Thomson Growth B. (ss) Formerly Thomson International B. (tt) Formerly Thomson Opportunity B. (uu) Formerly Thomson Target B. (vv) Formerly
 Piper Jaffray Sector Performance

ANNUAL TOTAL RETURNS (%)					TREND	PORTFOLIO DATA								RISK	TELEPHONE		
5 YEARS PRETAX		10 YEARS PRETAX		10 YEARS AFTERTAX		BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		TOLL-FREE (800)	IN-STATE		
8.4	6.6	18.1	15.3			High	11	22	MB	12	Philips Gloeilampen(2)	High	525-7048	CO	303-671-3200		
6.7	6.6					Average	28	36	SG	-22	Amgen(4)	Very high	525-7048	CO	303-671-3200		
						High	5	24	MB	1	Philips Gloeilampen(1)		525-7048	CO	303-671-3200		
0.1	-0.2	12.7	11.0			Low	5	36	MG	9	Placer Dome(4)	Very high	525-7048	CO	303-671-3200		
10.8	9.3	11.3	8.9			Low	15	17	LB	26	Microsoft(3)	Average	525-7048	CO	303-671-3200		
22.2	19.3					Very high	11	21	MB	-1	Philip Morris(1)	Average	525-7048				
9.7	8.2	11.1	9.1			Low	19	16	MB	16	United Healthcare(3)	Average	525-7048	CO	303-671-3200		
6.5	3.8	13.1	9.8			Average	15	22	MG	14	Advanta CI B(2)	High	525-7048	CO	303-671-3200		
10.5	8.4	15.0	11.6			High	2	21	MB	3	Houston Industries(1)	Average	525-7048	CO	303-671-3200		
8.7	7.1					Low	10	16	LV	14	AMP(3)	Low	525-7048	CO	303-671-3200		
10.8	8.1	15.6	13.9			Average	3	37	LB	11	Mitsubishi Petrochemical(2)	Very high	866-7778	MN	612-342-6223		
						Average	1	27	MG	10	Intl Game Technology(4)		332-3863				
						Low	3	15	MV	-2	General Motors(3)		662-8417	NY	212-309-8400		
						Average	7	15	MV	4	General Motors(3)		662-8417	NY	212-309-8400		
						Low	9	15	LB	-7	Mirage Resorts(3)		647-1568	NY	201-902-7341		
2.7	1.5	15.0	12.4			Very high	2	21	MB	-1	Hopewell Holdings(4)	High	647-1568	NY	201-902-7341		
						High	4	17	MB	-2	FNMA(3)		647-1568	NY	201-902-7341		
						Very high	16	24	MV	-14	Montedison(6)		647-1568	NY	201-902-7341		
8.5	7.5					Low	17	23	MG	14	Viking Office Products(2)	Average	647-1568	NY	201-902-7341		
						Average	9	22	SB	18	LDDS Communications CI A(5)		777-5143				
7.7	6.1					Average	12	14	LV	5	Entergy(4)	Average	777-5143				
10.5	9.2					Average	2	19	LB	14	Home Depot(4)	Average	777-5143				
ated						Average	2	18	LB	3	American Express(4)		451-8377				
16.6	14.7	13.3	11.8			Low	2	19	SV	13	Weillman(6)	High	999-3505	CA	415-362-3505		
8.2	8.1					Low	6	22	LG	9	Wal-Mart Stores(4)	High	882-2855	CA	818-351-4276		
						Very low	10	21	LG	13	Berkshire Hathaway(8)		882-2855	CA	818-351-4276		
6.4	4.2	10.3	7.5			Low	2	16	MB	-8	Merck(7)	Very low	767-1729	NH	603-431-8022		
ated							16	30	SG	15	Cobra Golf(2)		433-0051				
22.0	18.7					High	17	32	SG	8	America Online(2)	Very high	433-0051				
8.9	7.0					Average	1	19	MV	7	Eastman Kodak(3)	Low		MA	617-330-7500		
8.2	5.8	12.3	9.1			Low	10	18	LB	12	Royal Dutch Petroleum(2)	Low	523-8440	PA	215-670-1031		
8.5	6.5	12.1	9.2			Low	9	19	SV	21	Farmer Brothers(1)	Low	221-4268	NY	212-355-7311		
7.9	6.4					Very low	9	18	LB	5	General Electric(2)	Average	645-6561	NY	718-895-1206		
						Low	0	19	MB	1	General Motors CI E(2)		645-6561	NY	718-895-1206		
3.6	2.8	6.4	5.9			Average	11	21	MB	1	Property Trust America(1)	Very low	531-5142				
3.8	2.6	9.6	6.4			Low	6	18	MB	15	Wells Fargo(6)	Average	749-9933	FL	407-395-2155		
7.9	5.8	12.4	9.5			Very high	26	18	LB	-3	DuPont(2)	Very low	243-4361	CT	203-253-1000		
15.3	13.9					Very high	22	19	LB	1	McDonald's(2)	Low	243-4361	CT	203-253-1000		
7.7	4.7	12.6	7.9			High	2	20	LB	-1	Procter & Gamble(3)	Average	243-4361	CT	203-253-1000		
7.8	5.7	13.3	10.6			High	15	18	LB	1	American International Group(2)	Low	243-4361	CT	203-253-1000		
7.9	5.4	12.7	9.3			High	7	17	LB	-8	Eastman Kodak(3)	Very low	243-4361	CT	203-253-1000		
4.8	3.7					High	16	30	MB	0	Daiwa Securities(2)	High	243-4361	CT	203-253-1000		
9.9	7.4					Very high	49	21	LB	-1	Eastman Kodak(2)	Very low	243-4361	CT	203-253-1000		
7.1	4.8	11.4	8.4			Very high	27	20	LB	-2	Schlumberger(3)	Average	243-4361	CT	203-253-1000		
6.5	5.1	9.0	6.9			Very high	18	37	MB	-5	California Federal Bank CI A(2)	High	243-4361	CT	203-253-1000		
ated						Average	6	23	LG	6	Wal-Mart Stores(4)		576-8229				
8.0	6.3					High	0	20	SB	-3	Sbarro(2)	Very high	521-5411				
10.3	7.7					Average	0	18	LV	-6	General Motors(2)	Low	521-5411				
						Low	0	34	LV	3	Tokai Bank(2)		521-5411				
8.4	6.8	12.8	10.6			Very low	5	21	LB	30	AFLAC(8)	Average	334-3444	CA	310-551-0833		
6.9	5.8					High	7	21	LB	1	Amoco(4)	Average	426-0107	CT	203-352-4900		
9.7	7.5	15.3	12.8			High	6	20	LG	9	IBM(4)	Average	426-0107	CT	203-352-4900		
3.2	1.6					Average	8	30	LB	-3	La Rinascente(1)	High	426-0107	CT	203-352-4900		
21.0	19.4	18.8	16.5			Average	14	28	SG	26	EMC(8)	High	426-0107	CT	203-352-4900		
ated						High	4	22	MG	9	DSC Communications(4)		426-0107	CT	203-352-4900		
7.3	4.6	11.8	8.6			Very low	1	19	MB	26	National City(2)	Low	225-6292	MA	617-742-7825		
						Average	13	24	SB	7	Softkey Software Products(2)		225-6292	MA	617-742-7825		
						Low	0	16	MV	-2	Phelps Dodge(3)		225-6292	MA	617-742-7825		
9.7	7.1	14.2	11.7			Very high	15	32	SG	-5	Intervoice(5)	Very high	225-6292	MA	617-742-7825		
7.2	4.5	12.0	8.8			Average	3	18	MV	6	Healthtrust(3)	Low	225-6292	MA	617-742-7825		
6.9	4.5	10.1	6.9			Average	2	19	LB	-4	Atlantic Richfield(2)	Very low	225-6292	MA	617-742-7825		
ated						Very high	6	23	LV	-5	Astra CI A Free(5)		225-6292	MA	617-742-7825		
9.4	7.3	12.0	9.5			Low	4	17	SV	18	Interpublic Group(2)	Average	225-6292	MA	617-742-7825		
						Low	2	22	SG	23	Cisco Systems(2)		866-7778	MN	612-342-6223		
11.0	10.9					Very high	18	21	MB	4	United Healthcare(2)	Average	866-7778	MN	612-342-6223		
9.3	8.8					Very low	2	20	LB	25	United Healthcare(4)	Average	866-7778	MN	612-342-6223		
ated						Average	3	19	MB	3	Magma Power(1)		228-1024	WI	414-287-3808		
7.8	6.9					Very low	5	18	LB	15	General Electric(3)	Average	228-1024	WI	414-287-3808		
6.5	5.2					Average	7	20	MB	5	May Department Stores(3)	Low	228-1024	WI	414-287-3808		
ated							7	21	MB	2	Great Lakes Chemical(3)		228-1024	WI	414-287-3808		

DATA: MORNINGSTAR INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1994 RETURNS (%)				RANK (OBJ)
			ASSETS \$MIL	% CHG 1993-4	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE- TAX	AFTER- TAX	YIELD		
PORTICO SPECIAL GROWTH RET.	♦♦	Growth	388.5	9	No load	0.87	-2.0	-2.2	0.1	139	
PRA REAL ESTATE SECURITIES	♦	Specialty	103.4	-17	No load	1.15	3.0	-1.3	5.6		
PREFERRED GROWTH		Growth	241.1	67	No load	0.94	-1.1	-1.3	0.1	116	
PREFERRED INTERNATIONAL		Foreign	107.6	61	No load	1.36	3.3	1.9	1.1		
PREFERRED VALUE		Growth/income	148.6	21	No load	0.94	0.5	-0.4	1.8	52	
T. ROWE PRICE BALANCED	♦♦	Balanced	386.7	18	No load	1.00	-2.1	-3.7	3.8	2	
T. ROWE PRICE CAPITAL APPREC.	♦♦	Growth	648.1	24	No load	1.11	3.8	1.4	2.7	27	
T. ROWE PRICE EQUITY INDEX		Growth/income	266.4	69	No load	0.45	1.0	-0.2	2.7	39	
T. ROWE PRICE EQUITY-INCOME	♦♦	Equity-income	3143.9	13	No load	0.91	4.5	2.0	3.5		
T. ROWE PRICE EUROPEAN STOCK		Europe	355.5	41	No load	1.25	4.1	3.6	1.0		
T. ROWE PRICE GROWTH & INCOME	AVG	Growth/income	1219.8	8	No load	0.83	-0.1	-1.8	3.1	64	
T. ROWE PRICE GROWTH STOCK 🟢	AVG	Growth	2054.8	9	No load	0.83	0.9	-1.7	0.9	68	
T. ROWE PRICE INTL DISCOVERY	♦♦♦	Foreign	467.1	40	2.00*	1.50	-7.6	-9.1	0.4	4	
T. ROWE PRICE INTL STOCK 🟢	♦	Foreign	5982.0	60	No load	0.96	-0.8	-2.5	1.0	2	
T. ROWE PRICE JAPAN		Pacific	177.8	160	No load	1.50	15.1	12.7	0.0		
T. ROWE PRICE LATIN AMERICA		Foreign	195.4	NM	2.00*	1.99	-15.9	-15.9	0.0	6	
T. ROWE PRICE MID-CAP GROWTH		Growth	96.4	69	No load	1.25	0.3	-0.4	0.0	80	
T. ROWE PRICE NEW AMERICA GROWTH	AVG	Growth	636.8	6	No load	1.19	-7.4	-8.0	0.0	205	
T. ROWE PRICE NEW ASIA		Pacific	2061.7	20	No load	1.22	-19.2	-21.6	0.8	1	
T. ROWE PRICE NEW ERA 🟢	♦	Natural resources	987.7	34	No load	0.82	5.2	3.4	1.8		
T. ROWE PRICE NEW HORIZONS	AVG	Small company	1617.3	3	No load	0.95	0.3	-2.2	0.0	3	
T. ROWE PRICE OTC SECURITIES	♦	Small company	190.2	-4	No load	1.15	0.1	-2.8	0.2	3	
T. ROWE PRICE SCIENCE & TECH.	♦♦♦	Technology	844.7	81	No load	1.21	15.8	15.3	0.0		
T. ROWE PRICE SMALL-CAP VALUE	♦♦	Small company	415.8	-4	No load†	0.98	-1.4	-3.4	1.0	4	
T. ROWE PRICE SPECTRUM GROWTH		Growth	862.4	59	No load	0.00	1.4	-0.8	1.4	59	
T. ROWE PRICE SPECTRUM INCOME		Income	622.6	8	No load	0.00	-1.9	-4.2	6.7		
PRINCOR CAPITAL ACCUMULATION 🟢	♦	Growth	282.9	12	5.00	0.83†	0.2	-0.9	2.0	86	
PRINCOR EMERGING GROWTH	♦♦	Maximum growth	94.8	73	5.00	1.74†	3.0	2.8	0.1		
PRINCOR GROWTH	♦♦	Growth	117.2	36	5.00	1.30†	3.2	2.3	0.9	38	
PRINCOR WORLD	♦	Foreign	115.1	48	5.00	1.74†	-5.3	-6.1	0.5	4	
PRUDENTIAL ALLOCATION CONSERV. B (ww)	♦♦	Asset allocation	427.6	18	5.00**	2.00†	-3.6	-4.8	2.3	2	
PRUDENTIAL ALLOCATION STRATEGY B (xx)	♦	Asset allocation	326.0	-10	5.00**	2.03†	-5.2	-6.5	1.6	2	
PRUDENTIAL EQUITY B	♦	Growth	1891.0	10	5.00**	1.66†	1.6	0.0	0.9	55	
PRUDENTIAL EQUITY-INCOME B	♦	Equity-income	919.0	59	5.00**	1.75†	-0.8	-2.6	2.4	1	
PRUDENTIAL GLOBAL B	♦♦	World	388.2	45	5.00**	2.08†	-5.5	-5.9	0.0	3	
PRUDENTIAL GLOBAL GENESIS B	♦♦	World	183.4	91	5.00**	2.25†	-8.9	-9.0	0.2	4	
PRUDENTIAL GLOBAL NATURAL RES. B	♦♦♦	Natural resources	76.3	75	5.00**	2.65†	-5.6	-5.6	0.0	1	
PRUDENTIAL GROWTH OPPORTUNITY B 🟢	AVG	Small company	379.1	-1	5.00**	2.06†	-3.9	-5.8	0.0	6	
PRUDENTIAL MULTI-SECTOR B		Growth	164.5	51	5.00**	2.16†	2.7	-0.1	0.0	47	
PRUDENTIAL PACIFIC GROWTH B		Pacific	418.7	53	5.00**	2.12†	-9.5	-9.6	0.0	1	
PRUDENTIAL STRATEGIST B (yy)	♦♦	Asset allocation	164.3	-20	5.00**	2.13†	-7.0	-8.3	0.0	3	
PRUDENTIAL UTILITY B	♦	Utilities	3660.4	-23	5.00**	1.59†	-8.5	-10.4	2.8	1	
PUTNAM ASIA PACIFIC GROWTH A		Pacific	149.7	205	5.75	1.53†	-0.5	-1.4	0.0		
PUTNAM CORPORATE ASSET	♦♦	Income	118.6	-17	2.50	0.80	-3.8	-6.1	7.9		
PUTNAM EQUITY INCOME A	♦	Equity-income	303.7	-7	5.75	1.16†	1.3	0.1	3.8		
PUTNAM EUROPE GROWTH A		Europe	82.1	163	5.75	1.50†	6.4	6.1	0.0		
PUTNAM FUND FOR GROWTH & INC. A	♦	Growth/income	5768.2	11	5.75	0.95†	-0.3	-2.1	3.0	72	
PUTNAM GLOBAL GROWTH A	♦	World	1442.3	55	5.75	1.31†	-0.9	-1.8	0.0	2	
PUTNAM HEALTH SCIENCES A	AVG	Health care	793.0	2	5.75	1.12†	15.2	14.3	0.8		
PUTNAM INVESTORS A	♦	Growth	766.3	-7	5.75	0.99†	-3.2	-5.7	0.0	160	
PUTNAM MANAGED INCOME A	♦	Income	437.8	-18	5.75	1.09†	-1.2	-3.0	6.1		
PUTNAM NATURAL RESOURCES A (zz)	♦♦♦	Natural resources	119.6	2	5.75	1.24†	-2.8	-3.3	1.7		
PUTNAM NEW OPPORTUNITIES A		Growth	855.7	82	5.75	1.23†	3.4	3.1	0.0	32	
PUTNAM OTC EMERGING GROWTH A	♦	Small company	495.5	22	5.75	1.16†	2.2	0.1	0.0	2	
PUTNAM UTILITIES GROWTH & INC. A		Utilities	522.4	-20	5.75	1.08†	-7.0	-8.5	5.3		
PUTNAM VISTA A	♦	Growth	656.8	34	5.75	1.09†	-3.8	-4.0	0.0	173	
PUTNAM VOYAGER A 🟢	♦	Maximum growth	3362.9	24	5.75	1.10†	0.4	-0.7	0.0		
QUEST FOR VALUE A	AVG	Growth	223.0	-7	5.50	1.73†	0.9	-1.3	0.7	69	
QUEST FOR VALUE GLOBAL EQUITY A		World	148.0	8	5.50	1.95†	3.2	0.7	0.0		
QUEST FOR VALUE OPPORTUNITY A	♦♦	Asset allocation	163.6	31	5.50	1.78†	4.9	3.8	0.6		
QUEST FOR VALUE SMALL CAP A	♦♦	Small company	116.3	13	5.50	1.83†	-0.3	-1.0	0.0	3	
REICH & TANG EQUITY	♦	Growth	92.8	-13	No load	1.15†	1.7	-2.4	1.4	54	
RIGHTIME	♦♦	Growth/income	143.0	-14	No load	2.48†	0.8	-3.2	1.2	48	
RIGHTIME BLUE CHIP	♦	Growth/income	221.1	1	4.75	2.15†	2.2	-3.2	1.4	24	
RIGHTIME MIDCAP		Growth/income	67.8	9	4.75	2.26†	1.9	0.9	1.6	28	
RIVERSIDE CAPITAL VALUE EQUITY (aaa)		Growth	75.5	-6	4.50	1.36†	-3.2	-5.1	0.7	159	
ROBERTSON STEPHENS CONTRARIAN		Asset allocation	485.7	201	No load	NA †	-5.5	-6.1	0.0	3	
ROBERTSON STEPHENS EMERGING GRTH.	AVG	Small company	176.1	4	No load	1.60†	8.0	4.7	0.0		
ROBERTSON STEPHENS VALUE - GRTH. (bbb)		Small company	132.5	474	No load	1.55	23.1	22.7	0.0		
ROYCE EQUITY-INCOME	♦	Equity-income	81.7	0	1.00*	1.28	-3.3	-4.8	3.5	2	

* Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts. § Holding is less than 0.5% of assets.
 (ww) Formerly Prudential FlexFund Conserv Mgd B. (xx) Formerly Prudential FlexFund Strategy B. (yy) Formerly Prudential Growth B. (zz) Formerly Putnam Energy Resources
 (aaa) Formerly Riverside Capital Equity. (bbb) Formerly Robertson Stephens Value Plus.

Equity Funds

ANNUAL TOTAL RETURNS (%)				TREND	PORTFOLIO DATA							RISK	TELEPHONE	
5 YEARS PRETAX	5 YEARS AFTER TAX	10 YEARS PRETAX	10 YEARS AFTER TAX	BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)			TOLL-FREE (800)	IN-STATE
12.6	11.9				Average	11	20	SB	16	Cardinal Health(3)	Average		228-1024	WI 414-287-3808
7.0	3.9				High	0	25	SB	-7	South West Property Trust(6)	High		435-1405	
						1	24	LG	13	United Healthcare(4)			662-4769	
						7	25	MV	7	Hyundai Motor(2)			662-4769	
						16	16	LB	8	Monsanto(3)			662-4769	
9.3	7.0	12.5	8.7		Average	7	20	LB	3	General Electric(1)	Very low		638-5660	MD 410-547-2308
9.5	7.4				Average	20	23	MB	4	Philip Morris(3)	Very low		638-5660	MD 410-547-2308
					Very low	15	18	LB	5	General Electric(2)			638-5660	MD 410-547-2308
9.9	7.7				Average	9	18	LB	6	Philip Morris(2)	Low		638-5660	MD 410-547-2308
					Low	4	23	LB	8	Elsevier (Netherlands)(3)			638-5660	MD 410-547-2308
8.7	7.1	10.9	8.1		Low	8	20	LB	10	Calfed Bank Cl A(3)	Average		638-5660	MD 410-547-2308
9.6	7.7	13.7	10.7		Average	9	21	LG	23	FHLMC(5)	Average		638-5660	MD 410-547-2308
4.1	3.4				Average	4	24	SB	-1	Philippine Lg Dist Tel (ADR)(1)	High		638-5660	MD 410-547-2308
7.2	5.7	18.0	14.6		Low	4	30	LB	6	Wolters Kluwer (Netherlands)(2)	High		638-5660	MD 410-547-2308
					Average	5	42	MB	-2	Sekisui Chemical(2)			638-5660	MD 410-547-2308
					Very low	9	19		-24	Telefonos De Mexico A (ADR)(16)			638-5660	
					Average	9	25	SG	10	Smith International(3)			638-5660	MD 410-547-2308
11.2	10.4				Low	5	23	MG	19	CUC International(4)	High		638-5660	MD 410-547-2308
					Average	6	25	MG	-6	United Overseas Bank(3)			638-5660	MD 410-547-2308
5.3	3.3	11.6	8.8		Low	16	28	LG	19	Wal-Mart Stores(6)	Low		638-5660	MD 410-547-2308
13.2	10.5	11.9	9.1		Average	2	27	SG	27	CUC Intl.(3)	High		638-5660	MD 410-547-2308
8.3	5.2	10.8	7.6		Low	8	19	SB	19	Selective Insurance Group(2)	Average		638-5660	MD 410-547-2308
22.0	20.2				High	8	31	MG	21	Autodesk(5)	Very high		638-5660	MD 410-547-2308
11.8	10.5				Low	5	18	SV	13	La Quinta Inns(3)	Low		638-5660	MD 410-547-2308
					Very low	0	NA	LG	0	T Rowe Price Intl Stock Fd(20)			638-5660	MD 410-547-2308
					Low	15	NA		-6	T Rowe Price High-Yield Fund(22)			638-5660	MD 410-547-2308
7.6	5.8	12.0	9.3		Low	3	17	MV	5	Ford Motor(3)	Average		451-5447	IA 515-247-6833
13.7	13.2				Very low	10	19	SB	17	Health Systems International(3)	Average		451-5447	IA 515-247-6833
13.5	12.3	14.5	12.2		Very low	8	20	MB	23	Health Systems International(4)	Average		451-5447	IA 515-247-6833
7.8	7.1	12.3	9.4		Very low	3	19	MV	9	Svenska Handelsbanken Free(4)	Average		451-5447	IA 515-247-6833
7.9	5.8				High	15	18	MB	0	Dean Witter Discover(1)	Very low		225-1852	
6.8	5.0				High	38	17	LB	1	Royal Dutch Petroleum(2)	Low		225-1852	
10.4	8.0	14.3	12.0		Low	13	16	LV	11	Scott Paper(4)	Average		225-1852	
8.9	7.2				Average	4	21	MV	-2	Tenneco(3)	Low		225-1852	
4.4	4.3	13.1	12.2		Average	1	27	MG	13	Nichiei(2)	High		225-1852	
6.8	6.7				Low	12	26	SG	5	Liu Chong Hing Investment(2)	High		225-1852	
1.8	1.7				Low	4	31	MG	2	Tejas Gas(3)	High		225-1852	
10.7	8.9	12.2	10.1		Average	2	19	SV	4	Trinity Industries(3)	Average		225-1852	
					Average	8	20	MB	2	Motorola(2)			225-1852	
					Average	7	33	MG	4	Nichiei(3)			225-1852	
3.0	1.4	10.2	8.6		Very high	18	20	MB	5	First Financial Management(4)	Average		225-1852	
5.1	2.9	13.3	10.4		Low	4	15	MV	3	Telefonos De Mexico L (ADR)(3)	Low		225-1852	
					Average	4	37	MB	1	Daiwa Securities(2)			225-1581	
7.5	4.8	7.9	4.2		High	4	15	LV	-144	Philip Morris(1)	Very low		225-1581	MA 617-292-1000
7.6	5.3	9.8	6.0		High	2	17	LV	-45	JP Morgan(2)	Low		225-1581	MA 617-292-1000
					Average	10	21	MV	8	BASF(3)			225-1581	MA 617-292-1000
9.3	6.8	13.9	10.0		Average	4	17	LB	0	Philip Morris(3)	Low		225-1581	MA 617-292-1000
7.0	5.9	16.6	14.6		Average	7	24	MB	9	Sime Darby (Singapore)(1)	Average		225-1581	MA 617-292-1000
12.1	10.6	17.0	14.4		Low	3	21	LG	24	Abbott Laboratories(6)	High		225-1581	MA 617-292-1000
8.9	5.5	13.1	8.5		High	0	18	LB	6	General Electric(3)	Average		225-1581	MA 617-292-1000
8.3	5.3				Very high	3	16	LV	-6	Xerox(1)	Low		225-1581	MA 617-292-1000
3.7	1.2	9.4	7.4		Very high	4	27	MB	-7	Exxon(3)	High		225-1581	MA 617-292-1000
					Average	6	31	SG	16	Hospitality Franchise System(2)			225-1581	MA 617-292-1000
14.1	12.0	17.7	15.8		Average	3	32	SG	24	Liberty Media Cl A(2)	Very high		225-1581	MA 617-292-1000
					High	4	14	LV	-10	Entergy(4)			225-1581	MA 617-292-1000
11.2	8.6	14.8	11.6		High	8	21	MG	7	First Interstate Bancorp(2)	Average		225-1581	MA 617-292-1000
13.8	12.0	18.1	15.5		Average	9	26	MG	18	Lin Broadcasting(3)	High		225-1581	MA 617-292-1000
9.4	7.9	12.2	10.2		Low	10	17	MB	9	Exel(5)	Average		232-3863	NY 212-667-7587
					Average	15	25	LB	11	FHLMC(3)			232-3863	NY 212-667-7587
12.7	11.7				Low	21	15	MB	5	McDonnell Douglas(6)	Low		232-3863	NY 212-667-7587
12.9	11.5				Average	14	22	SB	6	Stratus Computer(3)	Average		232-3863	NY 212-667-7587
9.4	7.2				Low	6	17	MB	14	American Cyanamid(6)	Low		676-6779	NY 212-830-5220
8.4	5.7				Very low	100	NA		-1	Columbia Special Fund(2)	Very low		242-1421	PA 215-887-8111
7.3	5.2				Very low	100	18	LB	-2	General Electric(1)	Very low		242-1421	PA 215-887-8111
					Average	100	19	MB	-1	General Motors Cl E & S			242-1421	PA 215-887-8111
					Average	9	18	SV	2	Amdahl(5)			874-8376	
14.4	12.8				Very high	6	34	SG	-10	Santa Fe Pacific(5)			766-3863	CA 415-781-9700
					Very high	4	26	SG	6	Community Health Systems(2)	Very high		766-3863	CA 415-781-9700
7.6	5.4				High	1	21	MG	12	Vencor(6)			766-3863	CA 415-781-9700
					High	5	17	SV	-5	Argonaut Group(1)	Low		221-4268	NY 212-355-7311

DATA: MORNINGSTAR INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1994 RETURNS (%)				RANK
			ASSETS \$MIL.	% CHG 1993-4	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD	OBJ.	
ROYCE PREMIER		Small company	196.1	445	1.00*	1.46	3.3	2.6	0.8	2	
ROYCE VALUE	▲	Small company	166.7	-9	1.00*	1.90†	-1.6	-3.0	0.5	4	
RSI RETIREMENT CORE EQUITY	▲	Growth/income	141.3	-3	No load	0.99	1.3	1.3	0.0	33	
SAFECO EQUITY	▲	Growth/income	449.1	132	No load	0.85	9.9	8.1	1.9	1	
SAFECO GROWTH	▲	Small company	150.2	-8	No load	0.95	-1.6	-4.6	0.0	4	
SAFECO INCOME	▲	Equity-income	180.7	-10	No load	0.86	-1.1	-2.9	4.8	1	
SALOMON BROS. CAPITAL	▲	Growth	87.5	-23	No load	1.28	-14.2	-17.4	0.2	235	
SALOMON BROS. INVESTORS	▲	Growth/income	353.3	-9	No load	0.66	-0.8	-4.3	2.2	79	
SALOMON BROS. OPPORTUNITY	▲	Growth	108.8	-7	No load	1.22	0.8	-0.9	1.2	71	
SBSF	▲	Growth/income	108.0	-11	No load	1.19	-5.6	-7.5	1.4	126	
SCHAFER VALUE	▲	Growth	71.7	210	No load	1.48	-4.3	-5.8	0.9	180	
SCHWAB 1000		Growth/income	554.0	5	0.50*	0.51	-0.1	-0.7	2.1	66	
SCHWAB INTERNATIONAL INDEX		Foreign	137.7	30	0.75*	0.84	3.8	3.5	1.1		
SCHWAB SMALL CAP INDEX		Small company	67.5	NM	0.50*	0.55†	-3.1	-3.3	0.6	5	
SCUDDER CAPITAL GROWTH	▲	Growth	1294.5	-9	No load	0.97	-9.9	-10.8	0.0	227	
SCUDDER DEVELOPMENT	▲	Small company	589.5	-22	No load	1.27	-5.3	-7.1	0.0	7	
SCUDDER GLOBAL	▲	World	1131.3	29	No load	1.45	-4.2	-4.7	0.5	3	
SCUDDER GLOBAL SMALL COMPANY		World	239.3	22	No load	1.67	-7.7	-7.8	0.0	4	
SCUDDER GOLD	▲	Precious metals	125.7	30	No load	1.69	-7.4	-9.0	2.0		
SCUDDER GROWTH & INCOME	▲	Growth/income	1988.7	26	No load	0.87	2.6	0.2	2.9	18	
SCUDDER INTERNATIONAL	▲	Foreign	2299.8	26	No load	1.19	-3.0	-4.5	0.0	3	
SCUDDER LATIN AMERICA		Foreign	799.3	150	2.00*	2.01	-9.4	-10.4	0.0	5	
SCUDDER PACIFIC OPPORTUNITIES		Pacific	447.7	35	No load	1.93	-17.1	-17.3	0.6	1	
SCUDDER QUALITY GROWTH		Growth	108.5	-11	No load	1.25	-1.3	-3.5	1.0	122	
SEAFIRST RETIREMENT ASSET ALLOC.	▲	Asset allocation	144.6	-5	No load	0.94	-0.2	-2.4	3.3		
SEAFIRST RETIREMENT BLUE CHIP	▲	Growth	141.7	14	No load	0.95	2.1	-0.5	1.5	50	
SECURITY EQUITY A	▲	Growth	349.9	-5	5.75	1.06	-2.6	-4.6	0.0	148	
SELECTED AMERICAN	▲	Growth/income	503.0	11	No load	1.32†	-3.3	-5.3	1.6	107	
SELIGMAN CAPITAL A	▲	Maximum growth	172.3	-16	4.75	1.13†	-7.1	-9.9	0.0	2	
SELIGMAN COMMON STOCK A	▲	Growth/income	541.1	-3	4.75	0.84†	-1.9	-4.3	2.9	92	
SELIGMAN COMMUNICATIONS & INFO. A	▲	Technology	250.9	204	4.75	1.58†	35.3	32.3	0.0		
SELIGMAN GROWTH A	▲	Growth	557.5	-9	4.75	0.89†	-3.8	-6.6	0.2	172	
SELIGMAN INCOME A	▲	Income	309.3	-1	4.75	0.99†	-5.4	-7.1	5.7	1	
SENTINEL BALANCED	▲	Balanced	228.0	-1	5.00	1.16†	-3.6	-4.8	4.1	3	
SENTINEL COMMON STOCK	▲	Growth/income	842.0	-7	5.00	1.01†	-1.2	-3.2	2.9	84	
SENTINEL EMERGING GROWTH (ccc)		Small company	90.0	-17	5.00	1.56†	0.1	-4.4	0.0	3	
SENTRY	▲	Growth	75.7	-1	No load	0.87	-1.1	-2.9	1.2	115	
SEQUOIA	▲	Growth	1548.3	2	No load†	1.00	3.7	3.0	1.1	28	
SEVEN SEAS MATRIX EQUITY		Growth	138.3	55	No load	0.58†	-0.4	-1.2	2.3	101	
SEVEN SEAS S&P 500 INDEX		Growth/income	302.3	-2	No load	0.15†	1.3	0.3	2.8	32	
1784 GROWTH & INCOME		Growth/income	193.1	79	No load	0.35†	-0.2	-0.7	1.1	70	
SIERRA EMERGING GROWTH A		Small company	146.3	29	4.50	1.66†	-0.3	-1.0	0.0	3	
SIERRA GROWTH & INCOME A	▲	Growth/income	152.2	91	4.50	1.50†	0.1	-2.1	1.0	59	
SIERRA GROWTH A		Growth	122.1	40	5.75	1.75†	0.7	0.6	0.1	74	
SIERRA INTERNATIONAL GROWTH A		Foreign	122.3	48	4.50	1.69†	-1.3	-2.7	0.4	2	
SIFE TRUST	▲	Financial	410.2	-1	6.25	1.02	0.5	-1.5	4.2		
SIT GROWTH	▲	Growth	300.2	-6	No load	0.82	-0.5	-2.8	0.0	103	
SKYLINE SPECIAL EQUITIES	▲	Small company	202.0	-8	No load†	1.50	-1.2	-4.2	0.0	4	
SKYLINE SPECIAL EQUITIES II		Small company	89.5	64	No load	1.50	-1.5	-2.8	0.2	4	
SMALLCAP WORLD	▲	World	3482.7	28	5.75	1.15†	-2.9	-4.6	0.5	2	
SMITH BARNEY AGGRESSIVE GRTH. A (ddd)	▲	Maximum growth	176.4	-4	5.00	1.42†	-1.6	-2.5	0.0	1	
SMITH BARNEY APPRECIATION A (eee)	▲	Growth	1697.6	7	5.00	1.02†	-0.8	-2.8	1.7	109	
SMITH BARNEY CAPITAL APPREC. C (fff)		Growth	71.3	-20	1.00**	2.17†	-8.5	-8.5	0.0	221	
SMITH BARNEY FUNDAMENTAL VALUE B (ggg)		Growth	361.6	137	5.00**	2.06†	1.1	-3.2	1.2	64	
SMITH BARNEY GROWTH & INCOME A (hhh)		Growth/income	95.0	2140	5.00	1.49†	-4.3	-5.2	2.0	116	
SMITH BARNEY INCOME & GROWTH A	▲	Growth/income	559.6	-10	5.00	0.91†	-4.2	-5.5	3.6	113	
SMITH BARNEY INTL EQUITY A	▲	Foreign	519.2	81	5.00	1.29†	-8.9	-9.3	0.7	5	
SMITH BARNEY PREM. TOTAL RET. B (iii)	▲	Equity-income	1386.6	-2	5.00**	1.66†	2.9	0.5	7.9		
SMITH BARNEY PRINCIPAL RET. 1996 (jjj)	▲	Balanced	72.5	-21	5.00†	0.75	-0.3	-4.2	6.3	1	
SMITH BARNEY PRINCIPAL RET. 1998 (kkk)		Balanced	101.5	-26	5.00†	1.01†	-3.9	-6.9	5.4	4	
SMITH BARNEY PRINCIPAL RET. 2000 (lll)		Balanced	74.8	-23	5.00	1.14†	1.5	0.4	3.3		
SMITH BARNEY SPEC. EQUITIES B (mmm)	▲	Small company	93.2	-29	5.00**	2.25†	-6.3	-6.3	0.0	7	
SMITH BARNEY STRAT INVESTORS B (nnn)	▲	Asset allocation	219.5	-30	5.00**	2.02†	-2.1	-3.7	1.7	1	
SMITH BARNEY TELECOMM GROWTH B (ooo)	▲	Technology	191.1	42	5.00**	2.07†	-7.2	-7.3	0.3	1	
SMITH BARNEY TELECOMM INCOME (ppp)	▲	Utilities	67.8	-5	5.00†	0.95	-1.9	-4.7	4.0		
SMITH BARNEY UTILITIES B (qqq)	▲	Utilities	1501.6	-42	5.00**	1.54†	-10.1	-11.8	6.3	2	
SMITH BARNEY UTILITY A		Utilities	69.3	-40	5.00	1.00†	-8.6	-10.7	7.1	1	
SOCEN INTERNATIONAL	▲	Asset allocation	1822.5	28	3.75†	1.26†	2.5	1.6	0.6		
SOUTHERN OVERSEAS		Foreign	437.9	1119	3.75	1.37†	7.8	7.6	0.4		
SOUTHWEST VULCAN STOCK		Growth	118.9	221	5.50*	0.48	-1.7	-2.3	1.9	134	

* Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts. § Holding is less than 0.5% of assets. (ccc) Formerly Aggressive Growth. (ddd) Formerly Smith Barney Shearson Aggr Growth A. (eee) Formerly Smith Barney Shearson Appreciation A. (fff) Formerly Smith Barney Capital / Income. (ggg) Formerly Smith Barney Shearson Fundmntl Val B. (hhh) Formerly Smith Barney Shearson Growth & Inc A. (iii) Formerly Smith Barney Shearson Prem Tot Ret B. (jjj) Formerly Smith Barney Shearson Prin Ret 1996. (kkk) Formerly Smith Barney Shearson Prin Ret 1998. (lll) Formerly Smith Barney Shearson Prin Ret 2000. (mmm) Formerly Smith Barney Shearson Strat Investors B.

Equity Funds

ANNUAL TOTAL RETURNS (%)				TREND	PORTFOLIO DATA					RISK	TELEPHONE				
5 YEARS		10 YEARS		BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		TOLL-FREE (800)		IN-STATE	
PRETAX	AFTERTAX	PRETAX	AFTERTAX												
	7.4	5.6	10.8	8.5		Average	23	20	SV	1	Claire's Stores(2)	Low	221-4268	NY	212-355-7311
	7.1	7.0	13.4	13.3		Low	12	19	SV	19	Alleghany(1)	Average	221-4268	NY	212-355-7311
	13.0	10.8	16.2	12.8		Very low	4	17	LB	13	GTE(7)	Average	772-3615		
	10.0	7.5	11.9	8.9		Low	5	19	MB	10	Callaway Golf(5)	Average	426-6730	WA	206-545-5530
						Average	5	20	SB	23	Callaway Golf(12)	Very high	426-6730	WA	206-545-5530
	6.4	4.6	11.2	8.6		Low	2	18	LV	7	GTE(4)	Low	426-6730	WA	206-545-5530
	5.0	3.2	9.3	6.5		High	2	15	MV	-3	Deere(4)	High	725-6666	NY	212-783-2081
	8.2	4.7	12.0	7.9		Average	1	17	LB	10	Stop & Shop(3)	Average	725-6666		
	7.3	5.8	12.1	9.7		Very low	7	16	MV	42	Chubb(10)	Average	725-6666	NY	212-783-1301
	7.0	4.1	11.4	8.6		Average	1	22	MB	7	American International Group(6)	Low	422-7273	NY	212-903-1200
	12.3	9.3				Low	0	13	MV	-2	Fingerhut(3)	Average	343-0481	NY	212-644-1800
						Very low	1	19	LB	10	General Electric(2)		526-8600		
							1	32	LB	2	Royal Dutch Petroleum (BR)(2)		526-8600		
							1	20	SB	-3	Hillhaven \$		526-8600		
	6.6	4.2	14.2	11.3		Average	1	23	MG	7	Time Warner(5)	High	225-2470	MA	617-439-4640
	12.0	10.2	11.9	10.0		Average	3	25	SG	30	Cabletron Systems(5)	Very high	225-2470	MA	617-439-4640
	7.5	6.4				Average	9	28	LV	10	Canon(2)	Low	225-2470	MA	617-439-4640
						Average	7	31	SG	6	Tibbitt & Britten Group(3)		225-2470	MA	617-439-4640
	0.8	0.3				Average	0	29	SG	2	Pioneer Group(4)	Very high	225-2470	MA	617-439-4640
	10.2	8.0	14.3	10.9		Average	5	22	MB	8	United Technologies(3)	Low	225-2470	MA	617-439-4640
	5.6	4.2	16.2	13.4		Average	1	34	LB	10	Mabuchi Motor(1)	High	225-2470	MA	617-439-4640
						Low	9	23	MG	-7	Telefonos De Mexico L (ADR)(4)		225-2470	MA	617-439-4640
						Low	22	30	MG	2	Korea Electric Power(3)		225-2470	MA	617-439-4640
						High	0	18	LB	1	Chevron(3)		225-2470	MA	617-439-4640
	7.4	5.8				Average	2	20	LB	-3	Wal-Mart Stores(2)	Very low	323-9919	NY	206-358-6234
	7.9	6.8				Average	4	20	LB	2	Wal-Mart Stores(3)	Low	323-9919	NY	206-358-6234
	9.7	6.4	14.0	10.0		Average	8	19	LB	8	Monsanto(2)	Average	888-2461	KS	913-295-3127
	8.7	5.9	13.3	10.0		Average	1	15	LV	6	Wells Fargo(4)	High	243-1575	NM	505-983-4335
	11.2	8.5	13.3	10.5		Average	1	21	MG	21	Home Depot(4)	High	221-2783	NY	212-850-1864
	8.3	5.7	12.7	9.1		Average	5	21	LB	18	General Electric(2)	Average	221-2783	NY	212-850-1864
	24.2	20.6	22.2	18.3		High	14	22	SG	20	EMC(5)	Very high	221-2783	NY	212-850-1864
	8.3	5.3	12.8	8.9		High	4	23	MG	13	Home Depot(4)	High	221-2783	NY	212-850-1864
	9.0	6.5	10.8	7.5		Average	4	17	LV	-3	Shell Trans/Trading UK (ADR)(1)	Very low	221-2783	NY	212-850-1864
	7.1	5.3	11.0	8.6		Average	14	18	LB	5	JC Penney(1)	Very low	282-3863	VT	802-229-3900
	7.8	5.8	12.9	10.3		Very low	4	18	LB	38	General Electric(3)	Low	282-3863	VT	802-229-3900
							6	20	SB	10	Healthcare Services Group(3)		282-3863	VT	802-229-3900
	8.8	6.6	12.3	9.6		Low	3	18	MB	24	McDonald's(5)	Low	533-7827		
	11.5	9.1	14.3	11.2		Low	10	17	LV	32	Berkshire Hathaway(22)	Low		NY	212-245-4500
						High	1	17	LB	1	General Electric(3)		647-7327	MA	617-654-6089
						Very low	4	18	LB	0	General Electric(3)		647-7327	MA	617-654-6089
							5	NA		1	NA		252-1784		
	7.1	5.4				Very high	1	23	SG	8	Exide(6)		222-5852		
						High	3	17	LB	-3	Royal Dutch Petroleum(3)	Average	222-5852		
						Very high	24	21	MB	4	Gillette(5)		222-5852		
						Average	5	33	LV	1	Sakura Bank(1)		222-5852		
	10.4	8.3	13.3	10.9		Low	3	10	MV	24	Shawmut National(4)	High	524-7433	CA	510-937-3964
	11.4	10.2	15.4	13.6		Average	8	29	MG	18	Mercury General(3)	High	332-5580	MN	612-334-5888
	18.2	15.1				Average	5	12	SV	3	American Income Holding(2)	Average	458-5222	IL	312-670-6035
						Average	6	12	SV	0	Healthtrust(3)		458-5222	IL	312-670-6035
						Low	19	22	SG	9	Liberty Media CI A(2)		421-4120	CA	213-486-9200
	10.2	9.4	15.8	14.2		Very low	2	32	MG	46	Genentech(6)	Very high	451-2010	NY	212-720-9218
	7.6	6.3	13.8	12.3		Average	12	19	LB	9	Minnesota Mining & Mfg(3)	Low	451-2010	NY	212-720-9218
						High	0	18	LB	3	Lowe's(5)		544-7835	NY	212-698-5349
						High	32	23	LB	-3	Great Western Financial(3)		451-2010	NY	212-720-9218
						Average	4	17	LB	-3	British Airways (ADR)(3)		451-2010	NY	212-720-9218
	6.4	4.1	11.5	8.7		Average	8	16	LB	7	Royal Dutch Petroleum(4)	Low	544-7835	NY	212-698-5349
	11.2	10.3				Low	2	29	MB	4	Olivetti Group(1)	High	544-7835	NY	212-698-5349
	11.1	8.4				Low	20	14	LV	6	Philips(3)	Very low	451-2010	NY	212-720-9218
	7.5	3.8				Low	62	18	LB	5	DuPont(1)	Very low	451-2010	NY	212-720-9218
						Low	0	18	LB	3	DuPont(1)		451-2010	NY	212-720-9218
	8.0	7.5	9.7	8.8		Very low	60	29	SG	13	Genentech(4)		451-2010	NY	212-720-9218
						High	4	28	SG	17	Callaway Golf(11)	Very high	451-2010	NY	212-720-9218
						High	24	16	LV	0	General Motors(2)	Low	451-2010	NY	212-720-9218
						Low	4	31	MG	2	General Instrument(3)			NY	617-573-9410
	5.0	1.3	14.2	10.6		Very low	4	19	LB	62	Bell Atlantic(23)	High		NY	617-573-9410
	6.2	3.9				Low	0	14	LV	-9	Texas Utilities(3)	Very low	451-2010	NY	212-720-9218
						Average	3	13	MV	-6	GTE(3)		544-7835	NY	212-698-5349
	10.5	8.8	15.4	12.3		Low	15	23	SB	9	Bank for Intl Settlement(1)	Very low	628-0252	NY	212-399-1141
							42	24	MV	0	Bank for Intl Settlement Reg(2)		628-0252		
						Average	4	21	LG	1	Mobil(4)		239-7470		

Spec Equities B. (nnn) Formerly Smith Barney Shearson Strat InvestorB. (ooo) Formerly Smith Barney Shearson Telecomm Grth B. (ppp) Formerly Smith Barney Shearson Income. (qqq) Formerly Smith Barney Shearson Utilities B.

DATA: MORNINGSTAR INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1994 RETURNS (%)				RANK
			ASSETS \$MIL.	% CHG. 1993-4	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE-TAX	AFTER-TAX	YIELD		
STAGECOACH ASSET ALLOCATION	★★	Asset allocation	955.6	-5	4.50	0.82†	-2.8	-5.3	4.4		
STAGECOACH CORPORATE STOCK	AVG	Growth/income	244.8	-5	No load	0.97†	0.4	-1.1	1.9	51	
STAGECOACH GROWTH & INCOME		Growth/income	116.5	8	4.50	1.10†	-0.3	-1.5	1.5	71	
STAR RELATIVE VALUE		Growth/income	74.0	49	4.50	1.24†	-2.6	-3.3	2.2	91	
STATE ST. EXCHANGE	▼	Growth	200.6	-6	No load†	0.62	3.5	2.2	1.8	30	
STATE ST. INVESTMENT B		Growth/income	111.4	73	5.00**	1.58†	-4.4	-6.3	0.7	111	
STATE ST. RESEARCH CAPITAL B		Maximum growth	77.5	200	5.00**	2.16†	-0.5	-0.6	0.0		
STEINROE CAPITAL OPPORTUNITIES	▼▼	Maximum growth	172.3	4	No load	0.97	0.0	0.0	0.1		
STEINROE PRIME EQUITIES	★★	Growth/income	121.5	12	No load	0.90	-0.1	-1.7	1.3	61	
STEINROE SPECIAL	★	Growth	1167.7	0	No load	0.96	-3.3	-5.1	0.6	161	
STEINROE STOCK	AVG	Growth	302.6	-18	No load	0.94	-3.8	-7.4	0.6	171	
STEINROE TOTAL RETURN	★	Equity-income	215.1	-5	No load	0.83	-4.1	-5.8	4.8		
STI CLASSIC CAPITAL GROWTH INV.		Growth	154.0	-6	3.75	1.80†	-8.0	-9.1	0.6	211	
STI CLASSIC VALUE INC. STOCK INV.		Equity-income	72.2	49	3.75	1.15†	2.9	0.6	2.6		
STOCK & BOND A	★	Balanced	121.0	-2	No load	1.05	-1.9	-3.1	3.4		
STRATTON MONTHLY DIVIDEND	AVG	Equity-income	121.9	-31	No load	1.05	-12.1	-14.2	8.1		
STRONG ASSET ALLOCATION (rrr)	★★	Asset allocation	248.6	-2	No load	1.20	-1.5	-2.9	3.9		
STRONG COMMON STOCK	★★★	Small company	790.1	4	No load†	1.30	-0.5	-2.3	0.3		
STRONG DISCOVERY	★★	Maximum growth	388.4	29	No load	1.40	-5.7	-8.0	4.2		
STRONG GROWTH		Growth	106.0	NM	No load	1.60	17.3	16.9	0.9		
STRONG INTERNATIONAL STOCK		Foreign	257.8	101	No load	1.60	-1.6	-4.2	0.0		
STRONG OPPORTUNITY	★★	Growth	805.7	82	No load	1.40	3.2	1.7	0.5	31	
STRONG TOTAL RETURN	AVG	Growth/income	606.8	-4	No load	1.20	-1.4	-1.8	1.5	81	
SUNAMERICA BALANCED ASSETS B	AVG	Balanced	175.7	17	4.00**	2.20†	-2.6	-4.3	2.2		
SUNAMERICA BLUE CHIP GRTH. B (sss)	▼▼▼	Growth	71.0	-7	4.00**	2.29†	-4.8	-6.7	0.0	181	
TCW/DW BALANCED		Balanced	126.0	11	No load	2.10†	-9.7	-10.0	1.1		
TCW/DW CORE EQUITY		Growth	683.9	3	5.00**	1.93†	-7.8	-7.8	0.0	211	
TCW/DW LATIN AMERICAN GROWTH		Foreign	347.4	58	5.00**	2.89†	-23.7	-24.3	0.0		
TEMPLETON DEVELOPING MARKETS		Foreign	2000.9	44	5.75	2.17†	-8.6	-9.6	0.9		
TEMPLETON FOREIGN	AVG	Foreign	5305.8	50	5.75	1.14†	0.4	-1.7	1.7		
TEMPLETON GLOBAL OPPORTUNITIES		World	476.6	16	5.75	1.49†	-4.0	-8.2	0.4		
TEMPLETON GROWTH	★	World	5475.7	18	5.75	1.10†	0.8	-1.8	1.7		
TEMPLETON REAL ESTATE SECURITIES	AVG	Specialty	128.5	53	5.75	1.58†	-7.7	-8.2	1.7		
TEMPLETON SMALLER COMPANY GROWTH	▼	World	1275.9	-5	5.75	1.36†	-4.6	-5.3	1.4		
TEMPLETON WORLD	▼	World	5020.2	1	5.75	1.04†	0.9	-2.3	1.8		
THIRD AVENUE VALUE		Growth	183.4	48	4.50	1.15	-1.5	-2.1	1.5	121	
TOWER CAPITAL APPRECIATION	AVG	Growth/income	128.3	-9	3.00	1.09†	-2.6	-3.7	1.7	91	
TRADEMARK EQUITY		Growth	135.3	10	No load	0.74†	0.2	-1.1	1.8	81	
TWEEDY BROWNE GLOBAL VALUE		World	565.7	258	No load	1.65	4.4	4.0	0.0		
TWENTIETH CENTURY BALANCED INVSTRS.	AVG	Balanced	683.2	6	No load	1.00	-0.1	-1.4	2.8		
TWENTIETH CENTURY GIFTTRUST INVSTRS.	★★★	Small company	274.2	67	No load	1.00	13.5	11.8	0.0		
TWENTIETH CENTURY GROWTH INVSTRS.	▼	Growth	4158.0	-9	No load	1.00	-1.5	-5.6	0.2	121	
TWENTIETH CENTURY HERITAGE INVESTORS	▼	Growth	851.6	18	No load	1.00	-6.3	-7.8	0.3	191	
TWENTIETH CENTURY INTL. EQUITY		Foreign	1272.4	35	No load	1.90	-4.8	-6.1	0.0		
TWENTIETH CENTURY SELECT INVSTRS.	▼▼	Growth	3995.2	-20	No load	1.00	-8.0	-10.3	0.8	211	
TWENTIETH CENTURY ULTRA INVSTRS.	★★	Maximum growth	9850.8	18	No load	1.00	-3.6	-4.5	0.0		
TWENTIETH CENTURY VALUE		Growth/income	153.1	150	No load	1.00	4.0	1.7	2.4		
TWENTIETH CENTURY VISTA INVSTRS.	▼▼	Small company	820.2	3	No load	1.00	4.7	4.6	0.0		
UMB STOCK	★	Growth	120.9	6	No load	0.87	2.8	-0.2	2.4		
UNITED ACCUMULATIVE	▼	Growth	967.6	-6	5.75	0.70†	0.1	-2.4	1.8		
UNITED CONTINENTAL INCOME	AVG	Balanced	417.8	-1	5.75	0.87†	-0.4	-1.9	3.4		
UNITED INCOME	AVG	Equity-income	3144.3	3	5.75	0.72†	-1.8	-3.0	1.5		
UNITED INTERNATIONAL GROWTH	▼▼	Foreign	638.5	30	5.75	1.20†	1.8	-1.2	0.4		
UNITED NEW CONCEPTS	★★★	Small company	273.2	25	5.75	1.25†	11.3	9.2	0.1		
UNITED RETIREMENT SHARES	★★	Balanced	473.6	9	5.75	0.87†	-0.4	-2.1	2.5		
UNITED SCIENCE & TECHNOLOGY	AVG	Technology	496.4	11	5.75	0.96†	9.8	7.9	0.0		
UNITED SERVICES GOLD SHARES	▼▼▼	Precious metals	291.6	-14	0.10*	1.46	-2.7	-3.4	2.6		
UNITED SERVICES WORLD GOLD	▼▼▼	Precious metals	182.5	8	0.10*	1.53	-16.9	-17.0	0.2		
UNITED VANGUARD	▼	Growth	1017.7	6	5.75	1.05†	6.2	3.7	0.2		
USAA INVESTMENT BALANCED	★	Balanced	124.7	-2	No load	0.84	-2.6	-4.4	3.9		
USAA INVESTMENT CORNERSTONE	AVG	Asset allocation	841.3	10	No load	1.11	-1.0	-3.5	2.6		
USAA INVESTMENT GOLD	▼▼▼	Precious metals	158.5	-13	No load	1.26	-9.4	-9.4	0.1		
USAA INVESTMENT INTERNATIONAL	▼	Foreign	337.8	156	No load	1.31	2.7	1.0	0.0		
USAA INVESTMENT WORLD GROWTH		World	185.3	93	No load	1.28	0.6	0.0	0.0		
USAA MUTUAL AGGRESSIVE GROWTH	▼▼	Maximum growth	283.8	-2	No load	0.83	-0.8	-3.0	0.0		
USAA MUTUAL GROWTH	★	Growth	677.2	10	No load	1.04	3.3	-1.2	1.5		
USAA MUTUAL GROWTH & INCOME		Growth/income	150.5	58	No load	1.12	1.3	0.3	2.1		
USAA MUTUAL INCOME	★★	Income	1611.8	-17	No load	0.41	-5.2	-7.4	7.7		
USAA MUTUAL INCOME STOCK	★	Equity-income	1171.7	4	No load	0.73	-0.7	-2.8	5.6		
USAA MUTUAL EQUITY	AVG	Growth	120.9	1	4.50	1.07	0.2	-0.5	0.2		

† Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts. § Holding is less than 0.5% of assets. rrr: Formerly Strong Investment. (sss) Formerly SunAmerica Value B.

Equity Funds

ANNUAL TOTAL RETURNS (%)				TREND	PORTFOLIO DATA				RISK	TELEPHONE		
5 YEARS PRETAX	5 YEARS AFTER TAX	10 YEARS PRETAX	10 YEARS AFTER TAX	BW 10-YEAR ANALYSIS	TURNOVER	% CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)	TOLL-FREE (800)	IN-STATE
9.5	8.0				Average	0	18	LB	-6	General Electric(1)	Very low	222-8222
7.5	6.8	12.8	12.4		Very low	0	18	LB	26	General Electric(3)	Average	222-8222
					Average	4	18	MV	3	Tyco International(3)		222-8222
					Average	7	15	LV	5	Procter & Gamble(4)		677-3863 PA 513-867-5134
7.1	5.9	14.1	12.6		Low	2	21	LB		Capital Cities/ABC(5)	Average	562-0032
						2	22	LB	26	Abbott Laboratories(3)		882-3302 MA 617-357-7800
					High	10	25	MG	5	Hospitality Franchise System(3)		882-3302
8.6	8.3	12.2	10.4		Average	12	32	SG	20	Gartner Group(4)	High	338-2550 IL 312-368-7800
10.0	8.2				Average	14	22	LB	15	Microsoft(2)	Low	338-2550 IL 312-368-7800
10.9	8.7	15.7	12.5		Average	5	23	MB	14	Olsten(3)	Average	338-2550 IL 312-368-7800
9.6	7.2	12.9	10.4		Low	5	21	LG	21	Gillette(4)	Average	338-2550 IL 312-368-7800
8.2	5.6	11.0	7.9		Low	4	17	LB	7	United Dominion Realty Trust(2)	Low	338-2550 IL 312-368-7800
						6	17	LB	-5	General Electric(3)		428-6970
						2	20	LB	-3	American Cyanamid(2)		428-6970
6.7	4.9	9.5	6.9		Average	6	16	LV	5	Reebok International(2)	Very low	245-5040 PA 412-288-1900
6.1	3.6	9.3	6.1		Low	0	17	MV	-23	Health Care REIT(6)	Low	634-5726 PA 215-941-0255
7.4	5.0	9.3	6.3		Very high	33	20	MB	-2	Torchmark(1)	Very low	368-1030 WI 414-359-1400
19.0	16.7				High	11	24	MG	7	Bell Cablemedia (ADR)(2)	Average	368-1030 WI 414-359-1400
13.9	10.9				Very high	15	25	MG	-4	Orndorff Healthcorp(3)	Average	368-1030 WI 414-359-1400
					Very high	19	29	MG	5	Alco Standard(2)		368-1030 WI 414-359-1400
					High	8	27	MV	-6	Lend Lease(2)		368-1030 WI 414-359-1400
11.4	10.3				Average	13	23	MB	8	Bell Cablemedia (ADR)(2)	Low	368-1030 WI 414-359-1400
8.6	7.7	11.1	8.6		Very high	7	25	MG	0	Nucor(2)	Average	368-1030 WI 414-359-1400
7.8	5.1				Very high	2	19	LB	-5	Corning(1)	Low	858-8850 NY 212-551-5353
3.7	3.0				High	4	19	LB	-2	IBM(2)	High	858-8850 NY 212-551-5353
					Very low	17	15	LV	-13	Cifra (ADR)(3)		NY 212-392-2550
					Low	3	16	MV	8	Chrysler(4)		NY 212-392-2550
					High	1	24		-17	Telefonos De Mexico L (ADR)(9)		NY 212-392-2550
					Low	42	23	MG	3	Telefonos De Mexico L (ADR)(3)		FL 813-823-8712
9.5	7.4	17.7	15.2		Average	28	19	MV	5	DSM (Netherlands)(1)	Low	292-9293 FL 813-823-8712
					Average	5	20	MV	4	Peregrine Investments(3)		292-9293 FL 813-823-8712
10.7	7.8	14.9	12.1		Low	13	19	LV	12	HSBC Holdings (PLC) (HK)(1)	Average	292-9293 FL 813-823-8712
8.4	7.2				Low	26	19	SV	-6	Patten(3)	Average	292-9293 FL 813-823-8712
8.9	6.0	12.3	9.2		Low	9	17	SV	16	Telebras (ADR)(3)	Average	292-9293 FL 813-823-8712
8.7	5.4	13.5	10.2		Low	13	19	LV	14	Total Petroleum CI B(2)	Average	292-9293 FL 813-823-8712
					Low	14	17	SV	6	First American Financial(5)		443-1021 NY 212-888-6685
7.5	5.4				High	1	16	LB	4	AT&T(2)	Average	999-0124 PA 504-587-2708
					Average	5	17	LB	0	Saint Paul(3)		PA 502-566-3653
						11	20	MV	0	Unilever (Netherlands)(4)		432-4789
8.5	7.5				High	10	23	LG	5	Veba(2)	Average	345-2021 MO 816-531-5575
22.0	20.0	25.6	23.2		High	1	30	SG	25	Microchip(7)	Very high	345-2021 MO 816-531-5575
9.7	7.6	15.5	12.6		Average	5	23	LB	7	IBM(4)	High	345-2021 MO 816-531-5575
8.9	7.6				High	2	24	MB	4	Mylan Laboratories(3)	High	345-2021 MO 816-531-5575
					Very high	4	35	MB	1	Lyonnais Des Eaux-Dumez(4)		345-2021 MO 816-531-5575
5.7	3.5	12.8	10.2		High	2	23	LB	6	Caterpillar(4)	Average	345-2021 MO 816-531-5575
19.4	19.1	18.8	17.0		Average	7	31	LG	17	Oracle Systems(4)	Very high	345-2021 MO 816-531-5575
						3	20	MV	-4	Union Pacific(3)		345-2021 MO 816-531-5575
9.6	8.4	15.0	13.6		High	3	30	SG	26	Tellabs(6)	Very high	345-2021 MO 816-531-5575
8.2	6.2	11.4	8.7		Low	22	19	MB	5	Archer-Daniels-Midland(1)	Low	422-2766 MO 816-471-5200
6.7	4.3	12.4	8.4		Very high	15	19	LB	-6	Texaco(3)	Average	366-5465 KS 913-236-2000
8.0	6.5	11.6	8.8		Low	11	18	LB	4	General Motors CI E(3)	Low	366-5465 KS 913-236-2000
9.1	7.7	15.3	12.5		Low	5	18	LB	27	Motorola(3)	Average	366-5465 KS 913-236-2000
8.6	7.2	14.8	12.1		Average	2	27	MV	11	Nokia(5)	High	366-5465 KS 913-236-2000
19.9	19.1	14.6	12.9		Average	27	33	SG	27	United Healthcare(4)	Average	366-5465 KS 913-236-2000
9.5	7.7	11.9	9.1		Low	18	20	LB	9	Caterpillar(4)	Very low	366-5465 KS 913-236-2000
11.9	10.0	14.8	12.1		Average	14	27	MG	33	Informix(4)	High	366-5465 KS 913-236-2000
-9.9	-10.7	-1.8	-3.5		Low	-3	30		-48	Free State Consld Gold (ADR)(12)	Very high	873-8637 TX 210-308-1222
0.9	0.9				Low	5	35	SG	-11	Delta Gold(10)	Very high	873-8637 TX 210-308-1222
9.0	7.5	12.6	9.7		Average	13	25	LG	19	United Healthcare(4)	Average	366-5465 KS 913-236-2000
6.2	4.5				High	27	16	LV	0	Boeing(2)	Very low	382-8722
6.6	5.1	12.3	10.9		Low	12	24	MB	4	Weingarten Realty(1)	Low	382-8722
-1.5	-1.7	2.6	2.1		Low	3	31	MG	-53	American Barrick Resources(8)	Very high	382-8722
8.1	7.4				Average	7	29	LB	5	Minebea(2)	Average	382-8722
					Average	6	25	LB	5	Minebea(2)		382-8722
8.2	6.7	9.9	7.9		High	9	26	SG	11	Clear Channel Communications(3)	Very high	382-8722
9.3	7.1	11.4	8.7		High	0	17	MB	-2	Philip Morris(5)	Low	382-8722
					Very low	8	17	LV	0	BF Goodrich(3)		382-8722
7.7	5.1	9.9	6.4		Low	1	12	MV	-9	Public Service Enterprise(2)	Very low	382-8722
8.4	6.4				Low	1	17	LV	-3	Dow Chemical(5)	Low	382-8722
9.9	9.0				Low	2	23	MG	23	Informix(4)	Average	233-1136 MA 617-451-1912

DATA: MORNINGSTAR INC., CHICAGO, IL.

MUTUAL FUND SCOREBOARD

FUND	RATING	OBJECTIVE	SIZE		FEES		1994 RETURNS (%)				RAW O/C
			ASSETS \$MIL.	% CHG. 1993-4	SALES CHARGE (%)	EXPENSE RATIO (%)	PRE- TAX	AFTER- TAX	YIELD		
UST MASTER INCOME & GROWTH	AVG	Growth/income	103.9	28	4.50	1.07	-4.3	-6.1	3.0	111	
VALUE LINE	AVG	Growth	272.8	-18	No load	0.82	-4.5	-8.7	0.6	182	
VALUE LINE INCOME	▲	Income	131.6	-19	No load	0.91	-4.4	-5.6	3.4	21	
VALUE LINE LEVERAGED GROWTH INV.	▼	Maximum growth	264.8	-13	No load	0.90	-3.7	-4.4	0.5	21	
VALUE LINE SPECIAL SITUATIONS	▼▼	Maximum growth	90.2	-1	No load	1.13	1.0	-0.6	0.0	71	
VAN ECK ASIA DYNASTY A		Pacific	88.4	15	4.75	1.90†	-18.7	-19.3	0.6	21	
VAN ECK GOLD/RESOURCES	▼▼▼	Precious metals	175.2	-5	5.75	1.40†	-15.6	-15.6	0.0	51	
VAN ECK INTL INVESTORS GOLD (ttt)	▼▼▼	Precious metals	610.8	0	5.75	1.01†	-1.0	-2.3	1.1	21	
VAN KAMPEN UTILITY B		Utilities	78.0	-9	4.00**	2.04†	-10.4	-11.5	3.9	11	
VANCE SANDERS EXCHANGE	AVG	Growth	183.5	49	4.50‡	0.71	4.4	4.0	1.2	22	
VANGUARD ASSET ALLOCATION	▲	Asset allocation	1117.0	2	No load	0.50	-2.3	-3.5	4.2	31	
VANGUARD BALANCED INDEX		Balanced	392.0	11	No load	0.20	-1.6	-2.7	3.9	31	
VANGUARD EQUITY-INCOME	▼	Equity-income	868.8	-18	No load	0.43	-1.6	-3.1	4.5	31	
VANGUARD EXPLORER	▲	Small company	1092.6	38	No load	0.70	0.5	-1.0	0.4	31	
VANGUARD INDEX 500	AVG	Growth/income	9204.0	14	No load	0.19	1.2	0.2	2.7	31	
VANGUARD INDEX EXTENDED MARKET	AVG	Small company	956.9	9	No load	0.20	-1.8	-2.6	1.5	41	
VANGUARD INDEX GROWTH		Growth	79.3	61	No load	0.20	2.9	2.2	2.0	41	
VANGUARD INDEX SMALL CAP (uuu)	AVG	Small company	585.1	26	No load	0.18	-0.5	-1.6	1.4	81	
VANGUARD INDEX TOTAL STOCK MKT.		Growth/income	761.1	57	No load	0.20	-0.2	-1.0	2.4	61	
VANGUARD INDEX VALUE		Growth/income	298.4	67	No load	0.20	-0.6	-2.1	3.4	71	
VANGUARD INTL EQUITY EUROPEAN		Europe	711.8	31	No load	0.32	1.9	1.0	2.4	81	
VANGUARD INTL EQUITY PACIFIC		Pacific	688.6	49	No load	0.32	12.9	12.5	0.7	81	
VANGUARD INTL GROWTH	▼▼	Foreign	2947.2	64	No load	0.46	0.8	0.3	1.3	81	
VANGUARD PREFERRED STOCK	▲▲	Income	286.2	-25	No load	0.45	-7.9	-10.1	8.0	51	
VANGUARD QUANTITATIVE	AVG	Growth/income	584.8	14	No load	0.51	-0.6	-2.1	2.4	71	
VANGUARD SPECIAL ENERGY	▼▼	Natural resources	458.6	95	1.00*	0.19	-1.6	-2.7	1.6	71	
VANGUARD SPECIAL GOLD & PREC. MET.	▼▼▼	Precious metals	637.2	31	1.00*	0.24	-5.4	-6.1	2.4	61	
VANGUARD SPECIAL HEALTH CARE	▲▲▲	Health care	692.7	18	1.00*	0.25	9.5	7.2	1.5	41	
VANGUARD SPECIAL UTILITIES INC		Utilities	566.8	-27	No load	0.44	-8.6	-10.5	5.9	71	
VANGUARD STAR	▲	Balanced	3756.8	5	No load	0.00	-0.3	-2.0	4.0	81	
VANGUARD U.S. GROWTH	▲	Growth	2038.8	12	No load	0.52	3.9	3.5	1.2	22	
VANGUARD MORGAN GROWTH	AVG	Growth	1067.0	-6	No load	0.54	-1.7	-2.8	1.2	132	
VANGUARD PRIMECAP	▲	Growth	1472.4	87	No load	0.68	11.4	10.6	0.6	21	
VANGUARD TRUSTEES' EQUITY INTL.	▼▼	Foreign	1110.2	21	No load	0.32	5.3	4.1	1.7	81	
VANGUARD TRUSTEES' EQUITY U.S.	▼	Growth/income	114.8	5	No load	0.76	-3.9	-4.3	1.2	111	
VANGUARD WELLESLEY INCOME	▲▲	Income	5710.8	-2	No load	0.35	-4.4	-6.6	6.4	81	
VANGUARD WELLINGTON	▲	Balanced	8638.3	9	No load	0.39	-0.5	-1.9	4.5	81	
VANGUARD WINDSOR	▼	Growth/income	10858.1	4	No load‡	0.45	-0.1	-2.9	3.3	61	
VANGUARD WINDSOR II	AVG	Growth/income	7896.0	6	No load	0.39	-1.2	-3.0	3.4	81	
VICTORY BALANCED (vvv)		Balanced	126.9	NM	4.75	0.83	-1.7	-2.9	4.1	21	
VICTORY DIVERSIFIED (www)	AVG	Growth	263.0	3	4.75	0.89	3.9	0.0	2.1	22	
VICTORY EQUITY		Growth/income	122.3	18	4.75	0.39	-2.2	-2.6	1.3	91	
VICTORY INTERNATIONAL GROWTH (xxx)		World	77.3	125	4.75	1.34	2.7	1.3	0.0	11	
VICTORY SPECIAL VALUE (yyy)		Growth	115.0	NM	4.75	0.96	1.3	0.7	1.2	62	
VICTORY STOCK INDEX (zzz)		Growth/income	91.4	NM	4.75	0.50	0.9	0.2	2.4	41	
VICTORY VALUE (aaaa)		Growth	182.4	NM	4.75	0.90	0.2	-1.0	2.6	82	
VISTA CAPITAL GROWTH A	▲▲	Growth	543.2	106	4.75	1.50†	-1.3	-2.0	0.3	122	
VISTA GROWTH & INCOME A	▲▲▲	Growth/income	1340.8	30	4.75	1.39†	-3.4	-3.9	1.8	101	
VONTOBEL EUROPACIFIC	▼▼	Foreign	138.6	1	No load	1.64	-5.3	-5.5	0.5	71	
WADDELL & REED GROWTH	▼	Growth	80.7	143	3.00**	2.33†	12.8	12.1	0.0	71	
WADDELL & REED TOTAL RETURN		Growth/income	93.2	96	3.00**	2.10†	-2.1	-2.1	0.0	91	
WARBURG PINCUS CAPTL APPR COMM	▼	Growth	145.3	-9	No load	1.02	-2.7	-4.7	0.1	152	
WARBURG PINCUS EMERGING GR COMM	AVG	Small company	222.8	22	No load	1.20	-1.4	-1.4	0.0	11	
WARBURG PINCUS GROWTH & INCOME	▲▲▲	Growth/income	628.0	1722	No load	1.28	7.6	6.9	0.8	11	
WARBURG PINCUS INTL. EQUITY COMM.	AVG	Foreign	1551.7	206	No load	1.34	0.1	-0.9	0.5	11	
WASHINGTON MUTUAL INVESTORS	AVG	Growth/income	12668.3	0	5.75	0.69†	0.5	-1.3	3.6	51	
WAYNE HUMMER GROWTH	▲	Growth	87.7	-11	No load	1.07	-0.9	-1.6	1.4	112	
WEITZ VALUE	▲	Growth	107.7	1	No load	1.43	-9.8	-11.0	0.0	222	
WILLIAM BLAIR GROWTH SHARES	▲▲	Growth	182.2	22	No load	0.72	6.5	4.3	0.2	12	
WILLIAM BLAIR INTL GROWTH		Foreign	71.1	76	No load	1.88	0.1	-1.6	0.2	71	
WINTHROP FOCUS AGGRESSIVE GROWTH	▲▲	Maximum growth	147.4	81	4.00**	1.65†	-0.7	-2.0	0.0	11	
WOODWARD EQUITY INDEX RET.		Growth/income	332.1	-2	No load	0.18†	1.0	-0.7	2.7	31	
WOODWARD GROWTH/VALUE RET.		Growth	557.5	37	4.50	0.84†	0.5	-0.9	2.2	72	
WOODWARD INTRINSIC VALUE RET.		Growth	218.8	20	4.50	0.90†	-0.6	-2.0	3.0	102	
WOODWARD OPPORTUNITY RET.		Small company	510.0	54	4.50	0.89†	-3.3	-4.6	0.6	11	
WPG TUDOR	▼▼	Growth	159.2	-33	No load	1.26	-9.8	-12.0	0.0	222	
YACKTMAN	▼	Growth	295.1	106	No load	1.12†	8.8	7.7	2.2	11	
ZWEIG APPRECIATION A		Small company	218.2	-5	5.50	1.65†	-1.8	-2.9	0.4	11	
ZWEIG MANAGED ASSETS C (bbbb)		Asset allocation	582.4	51	1.25**	2.30†	-3.7	-4.1	1.5	71	
ZWEIG STRATEGY A	▲	Growth	427.0	5	5.50	1.34†	1.1	0.4	1.6	61	

Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts. § Holding is less than 0.5% of assets. (ttt) Van Eck International Investors. (uuu) Formerly Vanguard Small Capitalization Stock. (vvv) Formerly Society Balanced. (www) Formerly Society Diversified Stock. (xxx) Formerly Society International Growth. (yyy) Formerly Society Special Value Stock. (zzz) Formerly Society Stock Index. (aaaa) Formerly Society Value Stock. (bbbb) Formerly Zweig Series Managed.

Equity Funds

ANNUAL TOTAL RETURNS (%)				TREND	PORTFOLIO DATA						RISK	TELEPHONE	
5 YEARS		10 YEARS		BW 10-YEAR ANALYSIS	TURNOVER	%CASH	P-E RATIO	STYLE	UNTAXED GAINS (%)	LARGEST HOLDING COMPANY (% ASSETS)		TOLL FREE (800)	IN STATE
PRETAX	AFTERTAX	PRETAX	AFTERTAX										
7.3	6.0				Low	5	20	MB	0	John Wiley Sons CI A(2)	Low	233-1136	MA 617-451-1912
10.1	7.1	14.5	11.2		High	18	19	MB	4	McDonnell Douglas(2)	High	223-0818	NY 212-907-1500
6.7	4.3	10.4	7.0		High	9	19	MB	-2	US Treasury Note 3.875 (7)	Low	223-0818	NY 212-907-1500
9.5	6.9	13.5	10.7		Average	16	19	MB	22	Computer Associates Intl(3)	High	223-0818	NY 212-907-1500
7.8	6.7	7.8	6.5		Average	21	30	SG	27	Vencor(2)	High	223-0818	NY 212-907-1500
ated						7	22	MG	-2	HSBC Holdings(3)		544-4653	NY 212-687-5201
0.3	0.2				Very low	7	33	MG	-29	American Barrick Resources(11)	Very high	544-4653	NY 212-687-5201
2.3	1.2	8.9	7.2		Very low	3	28	MG	39	American Barrick Resources(5)	Very high	544-4653	NY 212-687-5201
ated						8	16	MV	-17	Southwestern Bell(2)		225-2222	IL 708-684-6000
8.7	8.2	13.0	12.2		Very low	2	19	LB		Intel(7)	Average	225-6265	
8.6	6.7				Average	2	18	LB	-1	AT&T(1)	Low	662-7447	PA 215-669-1000
ated					Low	0	19	LB	-2	AT&T(1)		662-7447	PA 215-669-1000
6.3	4.3				Low	1	18	LV	5	Bristol-Myers Squibb(3)	Average	662-7447	PA 215-669-1000
12.8	11.5	10.1	8.5		Average	13	22	SB	9	Dallas Semiconductor(2)	High	662-7447	PA 215-669-1000
8.5	7.4	14.1	12.2		Very low	4	18	LB	11	General Electric(2)	Average	662-7447	PA 215-669-1000
9.1	8.1				Low	2	21	SB	12	Berkshire Hathaway(2)	Average	662-7447	PA 215-669-1000
ated					Low	0	20	LG	3	General Electric(5)		662-7447	PA 215-669-1000
10.7	9.4	10.1	8.0		Average	2	21	SB	6	GFC Financial	High	662-7447	PA 215-669-1000
ated					Very low	2	19	LB	4	General Electric(2)		662-7447	PA 215-669-1000
ated					Low	0	16	LV	-2	Exxon(5)		662-7447	PA 215-669-1000
					Very low	1	22	LV	8	Royal Dutch Petroleum (Neth)(3)		662-7447	PA 215-669-1000
					Very low	0	45	LB	13	Toyota Motor(3)		662-7447	PA 215-669-1000
4.8	3.8	17.2	14.9		Low	1	31	LB	12	Intl Nederlander Groep(3)	High	662-7447	PA 215-669-1000
7.7	5.0	10.8	7.4		Average	2	NA		-17	Ford Holdings CI A Pfd(4)	Very low	662-7447	PA 215-669-1000
9.0	6.9				Average	4	16	LV	5	General Electric(3)	Average	662-7447	PA 215-669-1000
5.5	3.4	12.0	9.6		Very low	3	27	MB	-5	Exxon(4)	High	662-7447	PA 215-669-1000
4.3	3.5	10.5	9.3		Very low	10	34	MG	12	Free State Consld Gold (ADR)(4)	Very high	662-7447	PA 215-669-1000
15.6	13.6	20.0	17.9		Low	7	22	MB	16	Pfizer(5)	Average	662-7447	PA 215-669-1000
ated					Average	2	14	MV	-15	Nynex(5)		662-7447	PA 215-669-1000
7.9	5.8				Very low	18	NA	LV	1	Vanguard/Windsor II Fund(41)	Low	662-7447	PA 215-669-1000
10.1	9.6	12.8	10.5		Average	8	20	LG	12	General Electric(5)	Average	662-7447	PA 215-669-1000
8.0	5.5	12.5	9.0		High	6	18	MB	10	Motorola(2)	Average	662-7447	PA 215-669-1000
13.2	12.1	15.5	14.4		Very low	14	24	MB	22	Federal Express(4)	Average	662-7447	PA 215-669-1000
3.9	2.5	16.8	12.9		Average	3	29	MV	17	Onward Kashiyama(2)	High	662-7447	PA 215-669-1000
6.8	5.5	11.1	7.7		High	1	17	MB	5	Micron Technology(2)	Average	662-7447	PA 215-669-1000
8.5	5.9	11.8	8.6		Low	1	17	LV	-6	Texaco(2)	Very low	662-7447	PA 215-669-1000
7.9	6.1	12.4	9.7		Average	3	17	LV	8	Pfizer(2)	Low	662-7447	PA 215-669-1000
8.6	5.7	13.3	9.2		Low	7	16	LV	0	Citicorp(6)	Average	662-7447	PA 215-669-1000
7.8	5.8				Low	7	16	LV	4	Anheuser-Busch(4)	Average	662-7447	PA 215-669-1000
ated						8	17	LB		Abbott Laboratories(2)		539-3863	
9.4	7.0				Average	11	18	LB	1	Ford Motor(5)	Average	539-3863	
ated					Average	3	NA		-2	NA		539-3863	
ated					Average	7	31	MB	3	Mariner Marine Fund(3)		539-3863	
ated						7	19	SB		Michigan National(2)		539-3863	
ated						11	NA			NA		539-3863	
16.5	16.0					6	18	LB		General Electric(4)		539-3863	
14.9	13.4				Average	15	16	SV	1	Sunamerica(1)	Average	648-4782	
6.2	6.1				Average	19	16	MV	0	AlliedSignal(1)	Low	648-4782	
ated					Very low	1	29	MB	16	Korea Electric Power(1)	High	527-9500	
					Average	47	29	SG	13	Micron Technology(2)			KS 913-236-2000
ated					Low	8	16	LB	2	Caterpillar(3)			KS 913-236-2000
7.7	6.2				Average	3	27	MG	15	Intel(3)	Average	257-5614	NY 212-878-0600
12.9	12.2				Average	8	27	SG	16	Maxim Integrated Products(3)	High	257-5614	NY 212-878-0600
13.6	10.9				High	40	23	MB	0	Travelers(3)	Low	257-5614	NY 212-878-0600
10.8	10.0				Low	6	29	MV	3	DDI Pharmaceuticals(3)	Average	257-5614	NY 212-878-0600
8.0	6.4	13.9	11.4		Low	3	17	LV	15	GTE(3)	Low	421-4120	DC 202-842-5665
8.8	7.8	12.2	10.7		Very low	4	19	MB	19	Avery Dennison(4)	Low	621-4477	IL 312-431-1700
8.3	6.8				Average	18	22	MB	0	Tele-Communications CI A(5)	Low	232-4161	NE 402-391-1980
13.4	10.7	14.4	10.2		Average	9	28	MG	20	Alco Standard(3)	Average	742-7272	IL 312-853-2424
ated					Average	6	31	MB	0	Orix(2)		742-7272	IL 312-853-2424
13.4	10.9	14.3	11.1		High	2	18	SV	-7	Lydall(3)	Low	225-8011	NY 212-504-4000
ated					Low	1	18	LB	5	General Electric(3)		688-3350	MI 313-259-0729
					Average	13	17	LV	1	Schlumberger(3)		688-3350	MI 313-259-0729
					Average	7	18	MV	0	Figgie International CI A(3)		688-3350	MI 313-259-0729
					Low	5	17	SV	5	GFC Financial(2)		688-3350	MI 313-259-0729
8.3	3.9	12.3	9.0		High	1	25	SG	13	Informix(3)	High	223-3332	NY 212-908-9582
ated					Average	7	17	MG	2	Philip Morris(6)		525-8258	IL 312-201-1200
					High	33	11	SV	8	Equitable of Iowa(1)		444-2706	NY 212-635-9800
ated					Very high	62	25	LG	-3	Columbia/HCA Healthcare \$		444-2706	NY 212-635-9800
8.6	6.7				Average	60	11	MV	1	Micron Technology(1)	Low	444-2706	NY 212-635-9800

DATA: MORNINGSTAR INC., CHICAGO, IL.

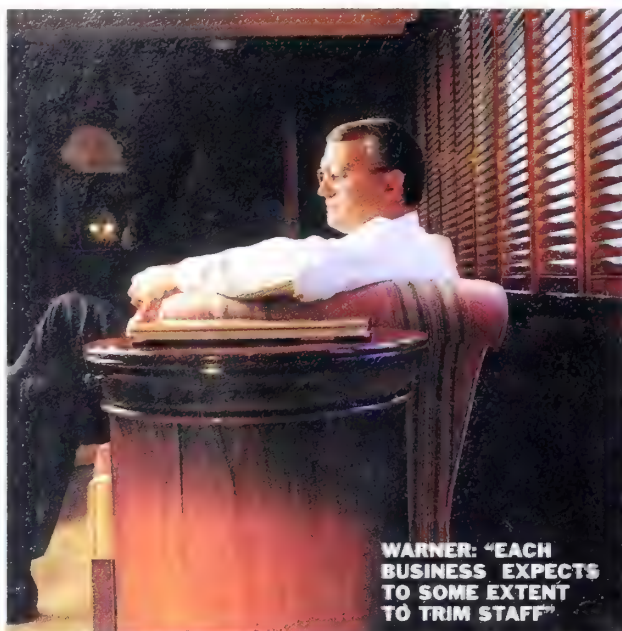
MOTHER MORGAN'S EMPTIER-NEST SYNDROME

The bank's culture could be wrenched by layoffs

While J.P. Morgan & Co. is not the biggest or most powerful U.S. commercial bank, it has always stood apart from its brethren, with a reputation as perhaps the classiest financial institution in America. A hallmark of its culture has been its maternalistic treatment of its employees. (Some used to nickname it Mother Morgan.) While other banks regularly trimmed large chunks of their workforces in bad times, Morgan always resisted.

Until now. Morgan is currently gearing up for its first widespread layoffs ever. BUSINESS WEEK has obtained a Jan. 24 internal memorandum from Chairman and CEO Douglas A. Warner III to "All Morgan colleagues" that outlines the bank's plans to cut back due to "difficult" market conditions. Warner says the bank is planning to slow down its expense growth and that staff cuts will ensue. "We have not set a target for staff reductions across the board," the memo says, with the "not" underlined for emphasis. But "since two-thirds of our costs are for people, each business expects to some extent to trim staff."

LITTLE LISTS. However nonspecific Warner's memo is, bank sources say the drive to cut costs is intense. Over the past decade, Morgan has hired thousands of people to help it become a major player in investment-banking businesses such as securities underwriting and trading. But now Morgan, like its competitors, is facing a slowdown in those businesses. As a result, at meetings during the second half of January, sources say, several dozen top Morgan executives were asked to prepare lists of people they could lose if necessary. Resulting cuts are expected to be completed during the first half of



WARNER: "EACH BUSINESS EXPECTS TO SOME EXTENT TO TRIM STAFF"

1995. Talk inside the bank is that parts of Morgan will face staff cuts of 10% or more. A bank spokesman declines to comment on any specifics of the planned cutbacks.

Morgan has plenty of company in its drive to reduce costs and payrolls. Investment banks, for example, are at least as vulnerable to poor capital-market conditions. Among investment banks, Merrill Lynch & Co. could eventually lay off close to 500 employees. CS First Boston has announced plans to let roughly 300 employees go worldwide. Even Goldman, Sachs & Co. has embarked on a program to reduce staff by 10%.

Commercial banks are also eliminating jobs. Last December, for example, Chem-

ical Banking Corp. announced plans to abolish 3,700 positions. Chase Manhattan Corp. is another money-center bank cutting back, offering voluntary retirement to roughly 2,600 employees. For many regional banks, sluggish demand for core products such as mortgages and a need to boost efficiency are prompting similar reviews of staffing levels. Fleet Financial, Corestates Financial, and Key Corp. have all hired consultants to help them reduce costs and possibly cut staff. Even foreign banks in the U.S. are pruning: National Westminster Bank has announced it will slash 500 jobs in the U.S. because it expects lower revenue.

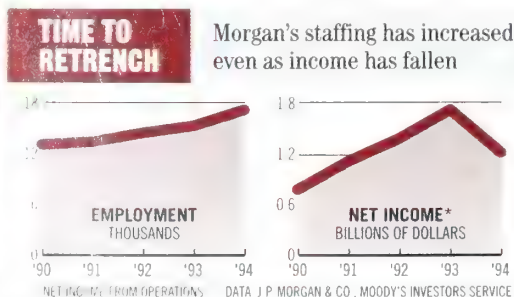
FREE LUNCH. Still, even with other financial institutions tightening their belt, it is a departure for Morgan to initiate such a widespread cost-cutting drive. The bank has long been regarded as an employer that takes superb care of its people—Morgan employees get a free lunch every day—and one that, more than most banks, holds on to employees through good markets and bad. As Morgan has reshaped itself over the past several years into more of a global investment bank, it has hired experienced outsiders, a sharp change from its longstanding practice of employing people for the long haul and promoting from within. Many employees say it has held on to much of its old ethos, although bank spokesman says the culture has evolved over the past decade. But bank-wide layoffs could wrench whatever remains of that culture.

To be sure, Morgan has reduced its workforce before. In 1989 and 1990, the bank embarked on a cost-cutting drive that resulted in a 9% reduction in employees in 1990. But most of those cuts were accomplished through attrition. "We've never ever had real layoffs," says one employee. Moreover, since 1990, Morgan has steadily expanded its workforce (chart). Its worldwide staff increased 12% in 1994, even as net income dropped by nearly 30%, from \$1.7 billion to \$1.1 billion. "They've been adding people a year long, but their revenues are falling apart," says David S. Berry, director of research at investment bank Keefe

Bruyette & Woods Inc.

Morgan's cutbacks, like those at many other firms, are probably a prudent response to difficult market conditions that will likely last for some time. But the need to retrench also is doubtless a painful reminder that even the best banks are no match for market cycles.

By Kelley Hollar
in New York



ENE G. MARCIAL

G FAVORITES SMALL CAPS

It's not cry for small-capitalization stocks, which got a sound drubbing last year. Investment pro F. Van Kasper, a small-cap advocate, says they are due for a smart snapback in 1995. Companies that had earlier post-record earnings got knocked in 1994. It makes the group even more attractive, with many stocks way off their highs," he argues. He thinks they earnings will keep rolling in 1995 and 1996.

Van Kasper, who heads a San Francisco investment bank, Van Kasper & did well last year: His small-cap portfolio, which gained 3.2%, outpaced Dow's 2.1% rise. Both the NASDAQ Value Line indexes, by contrast, ended some 6%. Part of Van Kasper's performance was due to a leap by one of its picks—Macrovision—and an 82% jump by First Sports. So what are Van Kasper's choices for 1995?

Some are hardly household names: Vision (ATVI), a maker of video and computer games; McFarland Energy (E), a conservatively managed oil-gas producer with more than 300

vs. losses in 1994 and 1995.

McFarland Energy, which just last September won a lawsuit against Chevron, bringing in \$16 million in compensatory damages and \$30.9 million in punitive damages, is expected to report earnings of 19¢ for 1994 and 35¢ in 1995. Van Kasper says it's one of the best energy plays around.

He is also high on Neurological Technologies thanks to a product now in clinical tests: corticotropin releasing factor (CRF), which Van Kasper says reduces swelling in cosmetic surgery. "This will be a big product for the company in two years," he says.

Odwalla produces more than 20 different fruit and vegetable drinks with "just-squeezed flavor," notes Van Kasper, who believes Odwalla's earnings will jump to 30¢ in 1995 and 50¢ next year, up sharply from last year's 12¢.

Van Kasper says all four stocks offer "ground-floor bargain opportunities."



VAN KASPER: *Four ground-floor buys*

Semmens says tests show that the Horizon matches the performance of emerging—and costlier—technologies, such as sodium-sulfur or nickel-hydride batteries. He maintains that a compact car equipped with the patented Horizon battery can travel more than 100 miles before it needs to be recharged. A minivan would have a range of 80 miles, he adds.

One big investor in Electrosources expects the company to post a loss this year, on estimated revenues of \$15 million to \$20 million. But he sees the company making money next year—about 50¢ a share—on sales of \$40 million to \$60 million.

BRIO TAKES TWO HEFTY SWIGS

Is there room for a newcomer in the crowded soft-drink and juice markets? "Definitely," says Herman Riepl, president of Brio Industries (BRIOF). A Vancouver (B.C.) bottler and packager of carbonated and noncarbonated beverages, Brio is a tiny speck in the business, but it has announced a three-year pact with two still-unidentified beverage biggies. Some investors say the deals will push Brio to profitability by next year.

David Jordan of J. W. Charles, a securities firm in Boca Raton, Fla., expects earnings per share of 32¢ on sales of \$46 million in the year ending Feb. 28, 1996, up from an estimated 15¢ on \$30 million in fiscal 1995. Because of the big contracts that were bagged by Brio, other drink companies have asked about concluding similar agreements, says Jordan, who has been accumulating shares. Brio got into the business by acquiring HPI Beverages in 1993 for \$10 million in cash and stock. And on May 31, 1994, Brio acquired JB Food Industries, which produces juices.

Why is Jordan so hot on Brio? He suspects that Coca-Cola and Quaker Oats are the mystery partners that have signed on. Quaker recently acquired fast-growing Snapple. Jordan thinks Brio is apt to sign more deals with these two, as it demonstrates the efficiency of its bottling and packaging facilities. Brio operates plants in Canada and is opening a fourth facility. Riepl declined to say who the partners were.

Jordan figures Brio, trading at 4½, could double in a year.

WHAT ONE PRO PROPOSES

COMPANY	RECENT PRICE	1994-95 RANGE	12-MONTH TARGET
VISION	6%	14½-3%	10
McFARLAND	6%	8½-4	12
NEURO. TECH.	4%	9½-2½	6
ODWALLA	13	15-10	20

SOURCE: BLOOMBERG FINANCIAL MARKETS, VAN KASPER & CO.

companies in California; Neurobiological Technologies (NTBI), a biopharmaceutical company with a network of scientist-shareholders; and Odwalla (ODWA), a large orange-juice company serving Northern California and Washington.

Macrovision is big in adventure videos and computer games. Some of its popular titles are Pitfall, Kaboom, and Return to Zork. In early January, the company signed a pact with Japan's Sega, which will pay royalties of up to \$5.5 million for Japanese versions of the game. Van Kasper expects the company to land in the black for the fiscal year ending Mar. 30, 1996, with estimated earnings of 30¢ a share,

GIVING ELECTRIC CARS A CHARGE

Want to bet on a company intent on speeding the advent of electric cars? It's not General Motors, Ford Motor, or Motorola. Try Electrosources (ELSI), a little-known battery maker whose shares trade at 2½.

Its claim to fame: revolutionizing the lead-acid battery so it can power electric vehicles, according to CEO Mike Semmens. He claims Electrosources' superbattery, the Horizon, provides everything electric cars need: quick acceleration, light weight, fast recharge, and long battery life.

The Horizon is so good, says one New York money manager, that Chrysler may announce soon it will use Electrosources' battery for its NS minivan—Chrysler's first electric vehicle. Also expected to use the Horizon is U.S. Electricar, whose vehicles have a Ford chassis. In mid-January, Solarmax, a Florida electric-vehicle maker, placed a \$2 million order for the batteries.



NEW CREW: Gearing up to make part for Chrysler in former Hangar 1

REDEVELOPMENT

THE BASE CLOSED. THE TOWN SURVIVED

Tiny Rantoul, Ill., has managed to hang on—and then some

For years, the tiny town of Rantoul, Ill., boasted an economy that was as shiny as a sergeant's shoes. As home to the Air Force's sprawling Chanute Technical Training Center, Rantoul could afford to pay cash for everything from fire engines to a new city hall. But in 1988, the town known for training military pilots looked set to nose-dive when the federal government announced it was closing 76-year-old Chanute, taking along thousands of jobs. "Everyone predicted we'd become a ghost town," says Katy Podagrosi, Rantoul's mayor since 1984.

These days, you won't find a whole lot of tumbleweeds in Rantoul. In the past 18 months since the base finally closed, town leaders have launched an aggressive recovery plan. By hawking real estate at cut-rate prices, Rantoul is remarking the once-government-owned property into a tax-paying boomplex. While still recovering from the exodus of 5,000 military workers and the money they spread

among the town's stores and diners, Rantoul is coming around. Some 20 companies have located or expanded on Chanute's three square miles, boosting the town's preconversion tax revenues by about 30%. And after losing 1,035 civilian jobs, Rantoul has added 1,000 new ones in a more diversified market. "Rantoul really pulled together," says Wallace Bishop Jr., senior project manager for the Defense Dept.'s Office of Economic Adjustment in Washington.

As the Pentagon prepares to announce the closing of some 30 military bases nationwide by Mar. 1, it's eager to point to places like Rantoul as evidence that there is life after the military. Defense officials have been coping with conversions

since 1988, when the Pentagon began closing 70 major bases and around 20 smaller installations, wiping out some 172,000 military and 95,000 civilian jobs.

The experience so far is mixed. It takes about six years to close a base completely. And many communities, large and small, are still struggling to generate the taxes to support the new land masses they inherited. They're also having trouble replenishing the lost jobs and income. Take Fort Sheridan, a suburban Chicago army base that in 1993 was slated for closure and shut down in 1993. Efforts to privatize the 700-acre lakeshore property have been slowed by clashing interests among its three bordering towns, two of which are affluent and one blue-collar. Meanwhile, the federal government is shelling out \$1 million a year to maintain the property. **ONE HORSE.** But a handful of communities, like Rantoul, have weathered the political fighting, cleanup rules, and tangled bureaucracies and transferred the bases into private hands. Rantoul has little choice. Unlike Fort Sheridan, Denver's Lowry Air Force Base, both of which benefit from the high property values of big-city neighbors, Rantoul was a one-horse town. Located about 120 miles south of Chicago, it was farmland until 1917, when the airfield tripled its population, to 23,000. Rantoul fought off Pentagon efforts to close the base in the 1970s but lost the recent battle.

After the base closed in 1993, Rantoul's mayor marshaled politicians and got \$3.5 million in federal aid to ease the transition. Mayor Podagrosi, backed by business and community volunteers, also kicked off "Make It Rantoul," a two-year campaign to lure jobs and tax dollars. They are targeting regional firms in distribution, manufacturing, and storage in need of new, low-cost space. "From the first year, I showed the property every day," says Ray Boudreaux, a tired Air Force officer who led the effort. Other selling points: Rantoul's low crime rate and skilled labor force.

Life After The Military

Like Rantoul, Ill., other towns are trying to turn the former bases into viable commercial projects.

WILLIAMS AIR FORCE BASE

Chandler, Ariz. Closed 1993. Employed 781 civilians, 4,000 military. Converting to an aviation hub, business and training center. Projecting 17,000 jobs.

DATA: DEFENSE DEPT., BUSINESS WEEK

LORING AIR FORCE BASE

Northern Maine. Closed 1994. Employed 1,311 civilians, 4,000 military. Providing financial services and training for the government. Hoping to create 1,000 jobs.

KINCHLOE AIR FORCE BASE

Sault Ste. Marie, Mich. Closed 1979. Employed 737 civilians, 3,074 military. Now three prisons, two work camps, and assorted manufacturing on site, creating 2,300 jobs.

companies were turned off by the remote location, a problem for former bases. The brass at Chicago-based United Airlines Inc. visited Rantoul several times before locating a new aircraft maintenance hub in Indianapolis instead. But Rantoul is pushing the area as more competitive by offering incentives to prospective employers: temporary tax breaks and other incentives. They can't get the land, since the land was a gift from the government. So Rantoul is offering lease space for manufacturing space on the 100-acre site for 25¢ to \$2.50 per square foot, compared with \$8 to \$10 in nearby Champaign-Urbana.

WINDOWS. Today, remnants of the old are scarce. In the old Hangar at Rantoul Products Inc. makes dashboards for Chrysler Corp. And Lowell-based J. B. Hunt Transport Inc., a trucker, has moved its training center into a former maintenance site.

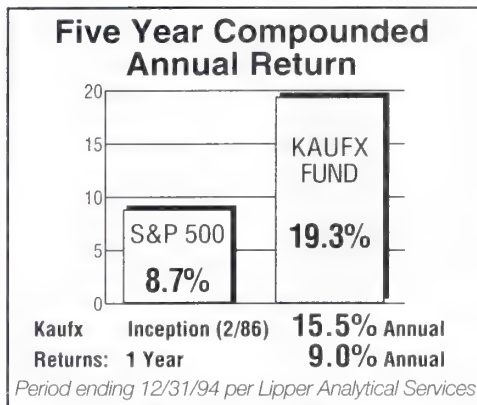
Caradco, a unit of Aluminum Company of America that makes wood-frame windows, Chanut's closing was serious. Caradco had been operating at the Rantoul factory since 1976 but had to get into the fast-growing market of custom-made windows. "Reopening the company had been part of our vision, but we didn't know how to do it physically," says Caradco president Alan Verploegh. Caradco expanded into the former 40,000-square-foot engine maintenance facility, adding 10 jobs, for a total of 900 workers. Closing has been an easier sell. Dealers have already snatched up a number of Chanut's 1,300 units of residential housing and are in the process of selling the rest. Since Rantoul never had a dime of taxes when the houses were in military hands, it's eager for a stream of property-tax revenues will come from its new housing market. Homes are selling for \$23,500 for a two-bedroom townhouse and \$30,000 for a three-bedroom home on a quarter-acre. Urbana-based Busey Bank, which bought two troubled Rantoul plants, is betting on a local boom. It already has \$3.5 million in Rantoul mortgages and expects an additional \$1 million by yearend. Busey President Harney bought the former base under a spread for about \$90,000. Rantoul hasn't quite shed its military past. The base still gets a single gas station and town clerks have the headache of meeting from its new tenants. The town has promised to reclaim a cargo terminal months ago. And Air Force vets still hang out at the Red Wheel restaurant. The transition is often painful, but Rantoul knows the peace dividend may be more than just a catchy phrase.

Ron Stodghill II in Rantoul, Ill., and Amy Borrus in Washington

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I-WAY TIE-UP ON CAPITOL HILL

Party politics are dimming the prospects for much-needed telecom reform

If there is one thing most Republicans and Democrats agree on, it's the need to reform the nation's 60-year-old telecommunications law. There's little argument that the rules limiting competition in the converging worlds of telecommunications, entertainment, and information—a \$1 trillion industry—must be reformed if the U.S. is to lead the way onto the Information Superhighway. So telecom legislation should be a sure thing, right?

Well, maybe not—because of partisan infighting. Consider what happened last year: The House, after six months of negotiations, passed a bipartisan deregulation bill by a 423-to-5 vote. Then, a month before the November elections, Senator Ernest F. Hollings (D-S.C.) killed the measure—after Senator Bob Dole (R-Kan.) added a list of “nonnegotiable” demands favoring regional Bell operating companies (RBOCs).

The mood on Capitol Hill is even more intensely partisan now, which makes ironing out the divergent Democratic and Republican approaches dicey. “People want to vote for competition,” says Scott Cleveland, an analyst at Washington Research Group, a unit of Mabon Securities Corp. “But we don’t know if, in three to five months, the Democrats and Republicans will be on speaking terms.”

GOP POWWOW. The bickering is derailing a lot more than the legislative process. Regulatory uncertainty is depressing telephone stock prices, holding up decisions on

billions of dollars worth of I-way investment, and slowing the rollout of such consumer goodies as interactive TV and a choice of local carriers. Plus, industry studies estimate deregulation could create up to 4 million jobs. “Every day that this act is not updated is a missed opportunity for us,” says Jamie DePeau, Washington spokesperson for Nynex Corp. “We’re very anxious.”

No wonder: Party intrigue is already overshadowing lawmaking. On Jan. 19 and 20, CEOs of many big phone companies met privately with House Republicans: No Democratic lawmakers were

invited. And the Senate Commerce Committee scheduled only Republican witnesses—Dole among them—at a Jan. 9 telecom hearing. As for the Democrats, Representative John D. Dingell (D-Mich.) reintroduced last year’s bill on Jan. 4 without first discussing it with Thomas J. Bliley Jr. (R-Va.), chairman of the House Commerce Committee, who oversees telecom legislation. “The kinds of things are bound to cause political differences,” says H. Bruce Thompson, CEO of LCI International Inc., a long-distance carrier.

Nonetheless, vows Larry Pressler (R-S.D.), chairman of the Senate Commerce Committee, Congress will pass a bill by July 4. To industry skeptics, that seems impossible. Even Gary V. McBee, upbeat chairman of the Alliance for Competitive Communications, an RBOC lobbying group, admits Pressler has “a pre-optimistic timetable.” Pressler dismisses those who say deregulation will again fall prey to infighting. “All I will say is this: The train is leaving the station. We welcome you on board.”

ANATHEMA. The big stumbling block is timing market entry. Last year’s bill would have opened local calling to competition immediately, while keeping the Baby Bells out of long distance and cable TV until there was some measure of erosion of their local monopolies. Such an approach is anathema to the RBOCs, which argue that long-distance carriers could hold them up for years with legal challenges. They want “date certain” on when they are free to enter



REPUBLICANS		DEMOCRATS
Push for a set date, perhaps Jan. 1, 1998, to let local and long distance rivals into each others' markets—favoring the Bells.	LOCAL VS. LONG DISTANCE	Favor preventing Baby Bells from entering long distance until there is proof of competition in local calling.
Senator Bob Dole has said he would like to repeal the 1992 Cable Act, ending rate regulation.	CABLE TV	Expected to fight off deregulation until there is real competition in cable markets.
To protect rural constituents, Republicans favor subsidies for rural phone companies and carriers of last resort for the poor and elderly.	UNIVERSAL SERVICE	Also eager to continue subsidies. Plus the White House wants a fund, paid for by carriers, to wire schools and libraries for the I-way.

ated industries, no matter how local competition really exists.

Republicans, who are generally allied with the Bells, favor the date-certain approach. A Senate Republican statement of principles calls for local competition immediately, with the Bells allowed into long distance on Jan. 1, 1998, no matter how big their local market share. If an RBOC can prove significant competition in its market before 1998, it will be able to apply to enter long distance just one year after the bill is passed.

Democrats, siding with long-distance carriers, fear this laissez-faire approach will allow the Bells to use their monopoly power to subsidize entry into the long-distance market while blocking local access. That wouldn't be hard, the theory goes, because the Bells own the "final mile"—connections to homes or office—of more than 90% of the nation. That's why Vice-President Al Gore, although a deregulation booster, insists that "the game should not begin until an arbitrary date without rules"—on the mistaken assumption that a market can replace a rule book."

COMMON GROUND. Expect clashes over deregulation, too. Some Republicans, including Senate Majority Leader Dan Quayle, want to repeal the 1992 Cable Act with its tough rate regulation. But Democrats are likely to dig in their heels. The law, which the Federal Communications Commission estimates has saved consumers some \$3 billion, is popular with voters.

The two parties have one patch of common ground: Both support federally mandated guarantees of universal service—requiring that cheap phone service be available to rural regions and poorest consumers, subsidized by the entire industry.

It's nail-biting time. Industry executives say the closed-door meetings of Republican lawmakers did not move the process ahead but did give them an opportunity to air views in a confrontational setting. And James H. Brown, AT&T's vice-president for federal legislation, thinks the Republicans are not being exclusionary—they are merely trying to coordinate their views before reaching out to the Democrats. "I do think that in the end we will see a bipartisan effort again as we did in 1994," he says.

Such an effort might pay off for everyone. Just look what competition has done for the folks at AT&T, says Thompson of LCI: "Since 1984, they've lost 60% of their market share, their earnings came down 60%—and they didn't have a single quarter of increasing earnings."

By Catherine Arnst in New York

TELECOMMUNICATIONS

MCI: A SMALLER FAMILY AND FEWER FRIENDS

It's losing customers to AT&T—and groping for a new strategy



PRESIDENT TAYLOR: "WE HAVE NOT DIED"

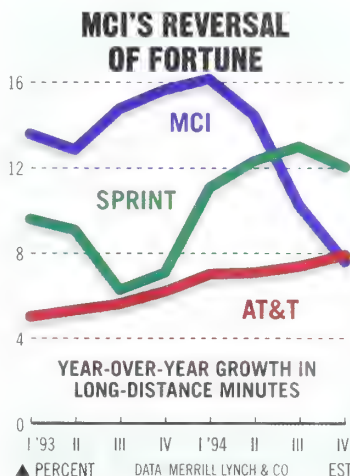
What in the world has happened to MCI Communications Corp.? Its reputation as a brilliant marketer is tarnished after losing 1.1 million customers to AT&T last year—almost 300,000 in December alone. Analysts figure that its fourth-quarter revenues dropped almost 1%, the first quarterly decline in five years. Its attempts to get into the wireless business fizzled. And since Wall Street has no clear picture of MCI's plans to diversify beyond the cutthroat long-distance business, the stock is hovering near a 52-week low of 17, almost 10 points below last March.

Investors may be unsettled, but MCI's leaders are still upbeat. Earnings in 1994, due Jan. 26, are expected to be up 15%, despite a 9% dip in the final quarter, analysts say. "We have not died," says MCI President Gerald H. Taylor. "We are not wringing our hands comforting one another about the situation." What MCI executives are doing is

trying to step back from an unrelenting battle for long-distance market share where the main weapon is discounts. MCI is searching instead for niches with better margins than in the commodity-like residential long-distance business. Says Executive Vice-President Timothy F. Price: "We want to take advantage of things on an opportunistic basis—new markets, new technologies."

Such as? So far, MCI has done little beyond announcing in January, 1994, a plan, dubbed networkMCI, to spend \$20

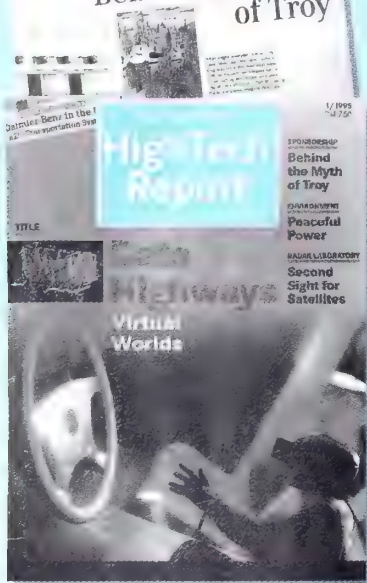
billion over six years to get into the wireless and local-calling business, while expanding overseas. But networkMCI is still mostly a blueprint, and there's more pressure for MCI to act. In a few years the seven Baby Bells are likely to gain entry into the long-distance business. As the only carrier with almost all its eggs in the long-distance basket, MCI is the most vulnerable to these well-heeled rivals.



DAIMLER BENZ

HighTech Report

Behind the Myth of Troy



Infobahns, supercomputers and multimedia are currently attracting widespread attention. In the latest issue of "HighTechReport", the Daimler-Benz group also focuses on these topics. Alongside the title story "Data Highways - Virtual Worlds", there are articles on the "People Mover", excavation work at Troy and much more...

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Information Processing

Diversification has become more urgent since MCI changed its rate strategy: Instead of leading the long-distance wars—as it has done in the past—MCI is following. AT&T last summer unveiled a lavish advertising campaign ridiculing MCI's four-year-old Friends & Family Plan. In September, AT&T upped the ante with a 30% discount to new customers for six months. MCI ignored the challenge with the result that growth in calling minutes slowed from a high of 14.7% in mid-1993 to an industry-lagging 7.5% in late 1994 (chart, page 147).

When strident "Shame on You, AT&T" ads failed to stem the tide, MCI finally responded on Jan. 5 with a "new Friends & Family" plan. It offers a 6% discount to AT&T's True USA—just enough, say analysts, to stabilize MCI's market share without triggering another AT&T rate cut. "Chasing pricing down a rat hole doesn't make any sense," says Price.

Problem is, MCI has yet to say what does make sense. Investors want to know—they especially want to know—what it will do with a \$4.3 billion cash hoard received from the sale of a 20% stake to British Telecommunications PLC on Oct. 1. "They have been very un-MCI-like in their deployment of capital," says Blake Bath, analyst at Sanford C. Bernstein. "Normally, they decide, and boom—off they go. They've known they were getting this money for more than a year... People aren't clear on what they are doing."

MCI is spending some. It has earmarked \$2 billion to build local fiber-optic networks in 200 cities by 2000. It says that six cities are up and running. MCI is also building a network in Mexico, budgeting \$450 million over three years. And last year, MCI paid \$30 million for a 20% stake in Los Angeles' Interactive Cable Systems, which sells cable and phone systems to apartment complexes, and \$20 million for a 20% stake in an in-flight phone company. And \$70 million went into developing and rolling out an information-management software package for businesses.

None of these businesses, however, matches the growth prospects of wireless. And MCI's wireless plan has yet to materialize. Last February, it agreed to pay \$1.3 billion for a 17% stake in Nextel Communications Inc., which wants to transform radio-dispatch systems into a cellular competitor. The deal fell apart over doubts about the quality of Nextel's service. Then, separate attempts to form wireless partnerships with Pacific Telesis, and BellSouth dissolved. MCI's reluctance to invest big but hasn't helped. Talks with a personal communications service (PCS) consortium by Bell Atlantic Corp. collapsed when the group wanted MCI to help foot

MCI Math, Part II.
40% = 13%

Friends & Family II. Big claims. Big disappointments.

AT&T True Math.
20% = 20%

AT&T True USA Savings. We say 20%. You save 20%.

SHAME ON YOU, AT&T.

Shame on you for charging the highest rates in the industry and then proclaiming the savings you offer as some "true" breakthrough to consumers.

Shame on you for mounting one of the most expensive and wasteful advertising campaigns in history. An expensive that your own stockholders and customers have paid for.

Shame on you for sending holiday cards with checks to MCI customers and not doing the same to your own customers.

And shame on you for marketing products under the banner of "true" and then doing an advertising campaign filled with "half truths."

Shame on you, AT&T.

We thought only a monopoly acted the way you do.

MCI
1-800-950-3090

MATH PROBLEM

MCI is no longer leading the unreeling battle for consumer market share where the main weapon is discount

bill for building it. thought lending its brand name was enough. "I fell apart because I egos," says Alb Grimes, an ex-MCI executive.

Now, MCI is in faltering mode. It plans to lease capacity and resell

banking on a glut of wireless capacity to drive down wholesale rates. That could make for lucrative margins, but reselling is not without risks. MCI won't be able to control the quality of the network nor will it be out in front with new services.

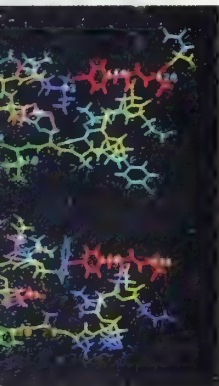
Analysts wonder if MCI's management is foundering or just trying to stay afloat. One thing in their favor, says L. B. Meltzer, of UBS Securities Inc.: "MCI excels when the chips are down. So companies flourish in a challenged atmosphere." And this situation is not if not challenging.

By Mark Lewyn in Washington with bureau reports

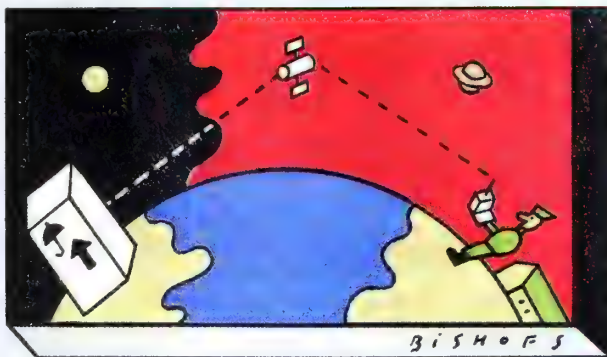
BY NEIL GROSS

GUINEA PIG THAT WON'T SQUEAL

ANIMALS TO TEST drugs and cosmetics are expensive and controversial. Soon, it may be unnecessary. Heartland Biotechnology in Davenport, Iowa, is racing to complete testing models of a creature few will ever be worked up about: yeast. As simulations of molecules show, at the top, yeast on the left, the cells are re-



ably similar to human cells, so they are a good model for toxicity. Heartland founder and CEO Maureen A. McKenney, a former Rutgers University chemical biologist, likes yeast because it's cheap, grows quickly, and is easy to manipulate. Heartland has applied for patents on its yeast-based drug research for diabetes and other diseases. It thinks yeast may reduce the need for animals when testing drugs for cancer, immune disorders, and fungal infections. But Heartland alone. Bristol-Myers Squibb Co. plans to invest up to \$45 million in New York's Cadus Pharmaceutical Corp. and its yeast-based drug screens.



MILITARY GOODS GET DIGITAL DOG TAGS

THE MILITARY GOT HIGH MARKS IN LOGISTICS DURING the gulf war. But one wheel of Operation Desert Storm proved creaky. Of the 40,000 intermodal containers ferried to the Persian Gulf, two-thirds had to be opened and inspected to determine what was inside. Many then had to be reshipped to their proper destination. To avoid a repeat of this snafu, the Pentagon is installing a \$70 million logistics-management system from Savi Technology Inc. that will let the military keep a tight rein on all materiel worldwide.

The Mountain View (Calif.) company's system is based on two-way "radio tags," about the size of a card deck, that are attached to shipping containers or to individual cartons inside. These SaviTags, powered by five-year batteries, can be tracked by satellite to determine location or reset for a new destination. A handheld "interrogator" reads containers' contents and addresses within a range of 300 feet, then triggers a beeper in one or more tags to help workers spot specific units. SaviTags are already used in the 2.5 million-square-foot facility at Kelly Air Force Base where jet engines are overhauled. "It's 'kanban' logistics," says Savi President Robert S. Reis. "You only build an asset when you need a replacement."

NEW DRUGS, THANKS TO DNA SCISSORS?

DNA, THE MASTER MOLECULE of life, may soon acquire a new role. Led by Scripps Research Institute biochemist Gerald Joyce in La Jolla, Calif., researchers have found a way to manipulate DNA as a "molecular scissors" that can snip other molecules. Using computers to scan 100 trillion strands of synthetic DNA, Joyce identified eight molecules whose coding enables them to cleave related RNA strands in as short a time as

one minute. Using this principle, Joyce thinks DNA-based drugs could be developed to cut the RNA in HIV and herpes viruses and kill them.

Others in recent years have developed similar scissors, based on RNA, that could snip genetic information out of cancer cells, preventing them from reproducing. But DNA, says Joyce, would be more effective than RNA because it is about 1 million times more stable. That means DNA-based drugs might stick around longer in the body and be administered in fewer doses than RNA-based compounds.

A NEW KIND OF SUPERPOWER IN GENEVA

HIGH-TEMPERATURE SUPERCONDUCTORS (HTS)—ceramic compounds that conduct electricity with no resistance at around the temperature of liquid nitrogen—are poised for a leap out of the lab. The Swedish-Swiss ABB Group, the world's largest maker of the sort of transformers used by utilities to transmit electricity, is building the world's first HTS transformer with support from Électricité de France and SIG, the electric utility of Geneva. When completed in 1996, the prototype will be tested in Geneva's electric power grid. The HTS transformer is anticipated to have much lower energy losses than conventional power-transformer technology. That advantage, combined with advances in HTS technology, is expected to make the transformer cost-competitive by the end of the decade.

INNOVATIONS

■ One group proposed growing mushrooms in the tunnel. Another, to study subsurface water flow. However, the most likely future use of the partially dug Superconducting Super Collider tunnel is: nothing.

The last of the more than \$2 billion pumped into the Texas physics project was spent putting steel caps on the openings so cattle won't fall down into high-tech Neverland.

■ IBM was America's top patent earner in 1994, with 1,298 of them. It was also the most active company in forming strategic alliances, reports Dataquest Inc. IBM made 31 of the publicly announced alliances or agreements between companies, followed by AT&T with 24.

QUIET STRIDES IN THE WAR ON CANCER

The immune system is slowly giving up its secrets to researchers pursuing vaccines

National Cancer Institute researcher Steven A. Rosenberg became a media sensation in 1985 when he achieved surprising success with cancer patients—including one complete cure—using an experimental technique called immunotherapy. His method made perfect sense: Since cancers can evade the immune system, why not flood the body with killer immune cells, along with special chemical messengers called cytokines that give

which could shrink existing tumors and reduce the odds of recurrence. Full-blown preventative inoculations probably are still decades away. But the past 10 years of intense research have produced a leap in molecular understanding.

MARROW HELPER. The first triumph of this deeper knowledge of immunology—long before any miracle drugs arrive—will be making life more comfortable for cancer patients. Doctors at

be performed on an outpatient basis

Within a few months, Sloan-Kettering's Malcolm A. S. Moore, who discovered G-CSF in 1984, hopes to start clinical trials on a more advanced technique growing precursors of immune and mature blood cells by culturing them in a cocktail of growth factors. Long-term says Moore, "I see no rationale for using bone marrow" to help chemotherapy patients.

All this is good news for Amgen Inc.

Immunex Corp., and other biotechnology companies that produce colony-stimulating factors (CSFs). According to analyst Steven C. Tighe at J.P. Morgan Securities Inc., CSF sales in the U.S. were roughly \$1.5 billion in 1994 and are growing by 12% to 15% a year. These drugs are a cry from cancer cure. But they could increasingly provide "a major advance in patient comfort and cost reduction," Tighe says.

Therapeutic vaccines are a tougher challenge for researchers. Tumors growing in the body produce antigens—molecules on the tumor surface that identify them as cancer. For reasons that scientists are

still struggling to understand, the antigens often fail to goad the immune system into action (box).

Such limited-use vaccines are under development at several biotech companies, including Montana's Ribi Immunochem. Some of them are trying to make existing tumor cells more visible to the body's killer T-cells, either by enhancing the chemical communication lines in blood and tissue, or by forcing tumor cells to display their antigens more clearly.

One-shot inoculations against cancer may still be decades away. But scientists are slowly unlocking secrets of the immune system. A better molecular understanding should yield improved immunotherapies. Here are some early advances:

Helping The Body Fight Cancer

ADVANCE Chemotherapy patients often need marrow transplants, but doctors can achieve the same result with transfusions thanks to improved "colony stimulating factors" for blood.

PLAYERS Amgen, Immunex

ADVANCE Doctors use everything from "gene guns" to retroviruses to insert specialized genes in cancer cells, thus boosting the immune system's ability to fight tumors.

PLAYERS Somatix, Vical, Pittsburgh Cancer Institute

ADVANCE Scientists are enhancing tumor-infiltrating lymphocytes, or TILs, which the body sends to tumor sites.

PLAYERS Applied Immune Sciences

ADVANCE Whole-body hyperthermia (WBH) raises patients' bodies to 107 degrees to help ward off the side effects of chemotherapy.

PLAYERS The Cancer Research Institute, University of Wisconsin

the body's weapons an extra kick. Dr. Rosenberg and others used one of the most promising of these compounds, interleukin-2. Sadly, the results, even 10 years later, haven't lived up to the initial hype.

Undeterred, scientists are still struggling to harness the human body's exquisitely complex immune system to fight cancer. They're priming patients' white blood cells to help them withstand chemotherapy. And they're tackling so-called "therapeutic vaccines,"

Memorial Sloan-Kettering Cancer Center in New York can now increase and harvest "stem cells" from chemotherapy patients' blood using genetically engineered growth factors such as G-CSF. When they are reinjected into the patient's bloodstream, these rare cells multiply and mature into key immune cells. That helps the patients withstand high doses of chemotherapy and radiotherapy. The technique is more effective than standard bone-marrow transplants. It also costs far less and can

ly attempts at therapeutic vaccination, most researchers agree, because they simply weren't specific enough. Doctors would inject patients with "chicken soup" of molecules, including mashed bits of the excised tumor and chemicals such as interleukin-2, interferon, and generic boosters called "adjuvants." These provoked often violent immune responses. The fury was rarely unleashed directly on the tumors.

FASTER AND SMARTER. Now, armed with better molecular maps, scientists say they can precisely target their assault. In 1992, Thierry Boon of the Ludwig Institute for Cancer Research in San Diego identified the first known tumor antigen from melanoma tumor cells. Since then, many scientists have identified these key molecules and even small protein fragments from them. In human clinical trials, some show promise of triggering T-cell reactions. Compared to the early therapeutic vaccines, says the NIH's Senior Vice-President Douglas L. Williams, "the next generation will be faster and smarter."

Researchers are racing to employ known cytokines—the chemical messengers that immune cells use to communicate—in gene therapies and to develop new ones. Of the 61 gene-therapy protocols that were approved by the National Institutes of Health in the past two years, "the largest single category is for cytokines as cancer treatments," says Nelson A. Wievel, director of the Office of Recombinant DNA Activities at the NIH.

Problems that confounded early vaccination efforts, however, still remain to be solved. Because immunotherapy is experimental, says Alain B. Schreiber, executive director of San Diego-based Vical Inc., doctors and pharmaceutical manufacturers have tested their ideas only on patients for whom conventional therapies failed. They often have large, solid tumors, to which the body, over time, becomes "tolerized." Says Schreiber: "Unlikely immunotherapy will be successful when the tumor burden is high."

An encouraging corollary: Any response in patients with advanced cancer offers hope that immunotherapy will be effective—especially for mop-up after surgery. When Dr. Gary H. Lin at the University of Michigan reported that a melanoma patient had tumor regression following a primary gene-therapy treatment, it was sufficiently impressive to initiate larger trials.

The most provocative data come from animal experiments. Although the tests have only limited relevance to human biology, the findings suggest

STANDING IMMUNE-SYSTEM THEORY ON ITS HEAD

Most researchers think the immune system springs into action when it encounters a foreign substance. This discrimination between "self" and "nonself" has been the central metaphor of immunology since the early 1900s.

The trouble is, it's wrong, says National Institutes of Health researcher Polly Matzinger. Last April, the 47-year-old head of the T-cell Tolerance & Memory section at the NIH's National Institute of Allergy & Infectious Diseases proposed a different metaphor. What spurs the immune system, Matzinger says, is a shout of "danger!" from cells dying in distress.

Matzinger argues that T-cells—the body's foot soldiers in the battle against cancer—don't care much if the antigens they encounter are foreign or "self." She, like other researchers, notes that T-cells require a signal from a critical white blood cell, called a dendritic cell, before they load their weapons and fire. Dendritic cells inhabit every tissue of the body, but they mostly lie dormant. To wake them up, cells nearby must call out in shock. "This [alert] is the initiation," Matzinger declared at a recent Cancer Research Institute seminar in New York. "Without it, you don't get an immune response. Ever."

"PROVOCATIVE." To colleagues, Matzinger's theory itself has been a wake-up call. "It's a provocative point of view that will influence many people to reexamine their work," says William E. Paul, head of the NIH's Office of AIDS Research. It has already sparked heated discussion at immunology meetings and swayed some pioneers in the field.

Kevin Lafferty, director of the John Curtin School of Medical Research in Canberra, Australia, says

he resisted the idea at first. Then Lafferty started to do some hard thinking about his own results in animal tissue transplantation. If he removed dendritic cells from a piece of skin and transplanted it to another animal, the graft would take, he says, even though the tissue was foreign. "My whole work was showing that the 'self/nonself' metaphor was wrong."



POLLY MATZINGER

Cells in shock send a danger call to dendritic cells—"without it, you don't get an immune response"

Matzinger, who spends as much as 18 hours a day in the lab and devotes her scant spare time to raising sheepdogs, says she already had doubts about the "self" metaphor as a graduate student. She was perplexed that T-cells don't attack "foreign-looking" substances that appear after puberty, such as milk proteins from newly lactating breasts.

Years later, at the NIH, a young oncologist named Ephraim J. Fuchs expressed similar doubts. "We knew the alert signal had to be danger," Matzinger recalls. "Then one day, in the bath, I realized it was caused by distressed cell death."

The theory's implications go beyond cancer vaccines. Matzinger says immunosuppressing drugs such as cyclosporine are often ineffective because they block signals between T-cells and transplants but don't block the alarm that cells in shock send to dendritic cells.

And what is that alarm, exactly? That's the missing piece in Matzinger's puzzle. It may be some kind of a chemical SOS, she says, but there are other possibilities. "I'm in the same position as a physicist who postulates a new particle and hopes she lives long enough for someone to find it," says Matzinger. Given the excitement she has already stirred up, a lot of people will probably help her look.

By Neil Gross in New York

new ways to attack wandering tumor cells that cause "metastatic" cancer. Johns Hopkins School of Medicine oncologist and geneticist Drew Pardoll says he has successfully vaccinated mice using mouse tumor cells that are genetically engineered to release the growth-factor GM-CSF. The cells, when irradiated, emit cytokines for at least one week, says Pardoll, helping the mouse produce killer T-cells that seek out and destroy metastatic tumors. Human trials should show if the technique is viable within two years.

The Holy Grail—still many years away—is a long-term, preventative cancer vaccine offering permanent protection against particular kinds of cancer. To create that, doctors must identify specific cancer antigens present on tumor cells of all the victims of that disease. Many researchers are focusing on cervical cancer, which has long been linked with human papillomavirus. Scientists at Johns Hopkins, Bristol-Myers Squibb Co., and elsewhere have immunized mice against papillomavirus antigens, then introduced tumor cells that express the antigen, and demonstrated protection.

WILD SWINGS. Even short of a universal vaccine, however, scientists may someday be able to help individuals whose genes place them at a high risk. Michael T. Lotze, professor of surgery and molecular genetics at Pittsburgh Cancer Institute, says it should be possible to sensitize the immune systems of such people by periodically administering "a wake-up call"—possibly, low doses of interleukin-12. It's not "a preposterous notion," he says. Animal tests are under way at Pittsburgh, using a "gene gun" that shoots DNA-clad gold particles into the skin to activate the dendritic cells.

Many scientists worry that too much attention to experimental results could once again trigger wild swings of public expectations and disappointment. George P. Canellos, chief of medical oncology at the Dana-Farber Cancer Institute in Boston, points out that only 50% of all cancers are curable today, and a decade of immunotherapies has done little to improve that ratio. Trumpeting early lab results raises false expectations among cancer patients, Canellos says, "followed by devastating disappointment."

The last thing any scientist wants is to repeat these wrenching cycles of hope and despair. But as the molecular understanding of the immune system races forward, therapeutic improvements seem certain to follow.

By Neil Gross in New York, with John Carey in Washington and Joan O'C. Hamilton in San Francisco

People

ENTREPRENEURS

THEY'RE BEARING THE GIFT OF SOUND

Two Coloradans have a promising new hearing device



LESS STATIC: Crouch and Waldron with HATIS

When United Airlines Flight 427 crashed in Colorado Springs in September, 1991, it was less than a block from Jo Waldron's house. But because Waldron is profoundly deaf—she was born 44 years ago with a 97% hearing loss—she didn't know what the flashing lights outside meant. Had there been a gas-main explosion? Should she bustle her sons to safety or stay put? Her frantic phone calls to local newscasters and a hospital—which she was able to make thanks to a prototype of a new device for telephones that she had helped develop—were curtly rebuffed with admonitions to "turn on the TV" or "listen to the radio."

That was just one of a lifelong series of frustrations at being cut off from a world saturated with telecommunications. In fact, Waldron and Shirley A. Crouch, her business partner, had decided a year

earlier that it was high time for the isolation of deaf people to end. The owners of Phoenix Management Inc.—founded to counsel people with disabilities and sponsor fundraisers at large companies—launched the company on a new track: developing low-cost technology for the handicapped.

Their initial product was an \$80 device dubbed HATIS, short for Hearing Aid Telephone Interconnect System. Waldron used it to call her mother and, for the first time ever, heard her mother's voice. Existing hearing aid-compatible phones are fine for people with slight-to-moderate hearing loss, says Waldron. But most of the 30 million hearing-impaired Americans can't understand what they hear,

she insists. "I've met thousands of deaf people, but only three of them use a hearing-aid-compatible phone." The reason: Background noises also get amplified, and these unwanted sounds can drown out the words.

MUSIC AND NEWS. HATIS is different because it plugs directly into a telephone jack in electronic equipment—TV sets, multimedia computers, cell telephones—or in a small adapter for regular phones. As a result, HATIS sends electronic signals straight to the user's hearing aid, avoiding the corruption of sound waves that travel through the air (box). Says Waldron: "It's really that simple."

Well, not quite. The signals actually go to a special earpiece, shaped like a flat banana, that sits atop the user's ear. Inside is a so-called induction coil that activates the hearing aid via

CONVENTIONAL HEARING DEVICE



Electronic signal
gets mechanical-
converted into
waves by a
er, which often
ts the sound

2 Sound waves travel through the air, where they are further contaminated by background noise

3 Hearing aid amplifies this hodgepodge, boosting the volume of not only the original signal but also the extraneous noises, often rendering everything unintelligible

HATIS DEVICE



1 The HATIS system plugs directly into a telephone or stereo, so the original electronic signals can travel straight to the HATIS device, which sits atop the user's ear

2 An induction coil in the HATIS earpiece is close enough to the hearing aid to transmit the signals to the hearing aid electromagnetically without amplification

3 The hearing aid amplifies signals that never passed through the air as sound waves, and HATIS produces distortion-free sound

magnetic field. And since the hearing aid amplifies an electromagnetic, not mechanical sound waves, volume can be increased while retaining clarity. As a result, people who never heard an intelligible sound listen to music and TV news.

Developing HATIS was surprisingly. Waldron knew what it should do, and he and Crouch were familiar with electronic gadgets for the noodle up a list of parts. They sold it to a local engineer in 1991. A few hours later, we had our first prototype," says Waldron.

It gobbled up two-thirds of their time and money was convincing telecommunications companies and phone makers HATIS is important. Waldron and Crouch have raised—and spent—\$700,000, selling their homes, cars, jewelry, and even some furniture. "We thought it would be rough," says Waldron. "So I sat my three sons down and told them what we'd be facing." Crouch backed her up, because they understood what it means for their children to be trapped in a soundless world.

When she had a miscarriage 10 months ago, it was her youngest son, age four, who called 911.

Determined to retain control of their lives, so they can keep their independence, Waldron and Crouch are hoping to grab some limelight at the annual meeting of the Telecommunications Industry Association in New Orleans, Feb. 1. Since Phoenix Management can't afford splashy advertisements, the partners are lobbying cellular manufacturers to help promote HATIS. If it happens, Crouch says sales could reach 10,000 systems this year, up from a few hundred to date. AT&T, Ericsson, and Motorola are among those offering cellular models with suitable for HATIS. "It's terrific technology," says CTIA President Thom Wheeler. "What it means is that

all people get the opportunity to take part in the wireless revolution."

Waldron was "manually deaf"—restricted to sign language and lip-reading—until she began intensive speech therapy when she was 21. "It took me 15 painful years" to amass a respectable vocabulary, she says. "Just learning to say 'ethical pharmaceutical' took four months. But we had a manually deaf kid who put on HATIS and learned to say 17 words in five minutes," she says. "His speech therapist was amazed. That's not supposed to be possible."

"THUMBS UP." HATIS has its skeptics. Dr. Stephen Epstein, an ear specialist in Silver Spring, Md., wants scientific tests to see whether HATIS helps profoundly deaf persons learn new words rapidly under controlled conditions. He believes HATIS will mainly benefit a small segment of the deaf population. Epstein has a moderate-to-severe impairment himself, and he found HATIS no better than a hearing-aid-compatible phone.

Still, the hard-of-hearing people who used a HATIS-outfitted cellular phone in informal tests run by Faris Howat, technical support director at Nynex Mobile Communications Co., "gave it two thumbs up," he says. Mary G. Whalen, owner of Sound Waves, a New Rochelle (N.Y.) mail-order company that sells products for the deaf, says she always had difficulty with phones until she tried HATIS.

Motorola Inc. is providing a HATIS-equipped two-way radio to Shelley Beattie, the deaf crew member of the America's Cup yacht, now competing in the

America's Cup trials. "If it works there, we think it would benefit the hard of hearing in lots of other situations," says David S. Weisz, manager of sports marketing. One might be sounding the fire alarm in office buildings.

Finally, HATIS can enable deaf people to hold down jobs as telemarketers and help-desk operators. Plantronics Inc., a leading manufacturer of telephone headsets, has already built a plug-in

socket that will accommodate HATIS. Michael W. Erbe, special-projects manager, expects that many companies will snap up the system to comply with the Americans with Disabilities Act, which requires large companies to employ a certain number of disabled workers.

Waldron and Crouch started their company in 1987, after President Ronald Reagan named Waldron that year's Outstanding Disabled American, in honor of her work with United Way and other charitable organizations, plus her longtime championing of the cause of the handicapped. In 1988, she was named to the President's Committee on the Employment of People with Disabilities.

The partners have a long list of new products they want to develop, but they're short on cash. So, until HATIS catches on, Phoenix Management will probably survive on a shoestring. But Crouch, the duo's penny-pincher, is resigned to fat phone bills. "Now that Jo can use the phone, you can't shut her up," she says. Retorts Waldron: "Hey, I'm just making up for lost time."

By Otis Port in New York

Waldron and Crouch have raised—and spent—\$700,000, selling their homes, cars, jewelry, and even some furniture

EDITED BY AMY DUNKIN

NO-SWEAT SOFTWARE FOR THE TAX TRIALS



Time was when using tax-preparation software was almost as time-consuming as preparing your 1040 by hand. Whatever gains the programs offered by automating tedious calculations and putting dozens of obscure Internal Revenue Service forms and schedules at your fingertips were offset by the difficulties—particularly for computer novices—of navigating the software.

To their credit, the developers of tax software have made their programs much more user-friendly. The latest editions of TaxCut and TurboTax, the top-selling tax software, have undergone extensive redesigns that let users move around with greater ease.

And more programs are being offered on CD-ROM, a format that should be perfectly suited for tax use. Seasoned filers gain access to meaty tax guides, while neophytes may appreciate the full-motion video clips of leading tax experts explaining the IRS code and offering advice. Unfortunately, while the CD-ROM versions showed improvements over last year's first efforts, most still haven't tapped the full potential of multimedia.

TIE-INS. Despite the advances, most tax software remains useful largely where tax situations are fairly straightforward. Returns involving such complexities as self-employment, partnership income, or

passive investment losses may still require the services of a pro. But even if you hire an accountant, you might keep down the cost by using software to prepare a first draft. At the least, you'll be better organized when your accountant starts the meter running.

Both TaxCut and TurboTax are promoting links to their corporate parents as selling points. TaxCut buyers who later conclude they need professional help can apply the full cost of the software toward the fee charged by H&R Block, which acquired TaxCut's parent—Meca Software—about a year ago. What's more, TaxCut users can call the nearest H&R

Block office for answers to tax-related questions and free help if they're audited.

TurboTax offers a similar tie-in, with a \$25 credit good at any of 10,000 participating tax preparers. But much of TurboTax's appeal is its integration with its sister software, Intuit's Quicken personal finance program. This year, TurboTax makes it easier for Quicken users to import data—such as deducted medical expenses—into tax return.

Still, TurboTax and TaxCut stand up well on their own. In response to user complaints, both now make it easier to leave the "interview" process and skip other sections. "Last year, people felt like they were

YOUR TAXES

g a tightrope," admits Jacobsen, Meca's marketing vice-president. "If they from the interview to ms, they couldn't figure how to get back." Integrating TaxCut has been simpler with a new feature that groups the various steps and functions under notebook-style tabs. As it, users of TaxCut's previous version can jump to any tax topic with the clicks of the mouse. When tax season's over, a "uninstall" step now deinstalls the program—save for the file that retains key data for next year—from the drive. That comes in handy now that most tax programs hog up to 15 megabytes of drive space, versus the average 6.5 megabytes for older versions.

IMPROVEMENTS. Combining these improvements once again with TaxCut the program for taxpayers. But not filers may find TaxCut's handling still too tight. Rival TurboTax allows veteran users to navigate quickly. This version also has a new notebook-style interface, with 15 more screens and does a better job of transferring data from its screens to other programs. TurboTax has added an "undo" feature of

er plus: TurboTax cleaned up a cluttered interface, eliminating features of earlier versions. For instance, "errors and omissions" were intended to catch mistakes that could trigger a penalty—had pointed out mistakes but left it to the user to go back and fix them. TurboTax takes the user to the offending item, allowing on-the-spot corrections. A year ago, Computer As-

sociates International offered its fledgling Simply Tax for just the \$8 shipping cost. The promotion seemed to pay off—800,000 copies were distributed. Unfortunately, it doesn't appear that this year CA has given customers much reason to come back. The 1995 edition debuts a new interface that's much less intuitive than last year's. Despite incorporating tips drawn from the *Ernst & Young Tax-Saving Strategies Guide*, the overall level of advice it offers pales beside that of rival programs.

Bargain-conscious filers might want to consider Personal Tax Edge, at \$19 from Parsons Technology. While not as rich in features as TaxCut and TurboTax, Tax Edge is a sturdy program

those for TurboTax and TaxCut.

Indeed, Tax Edge is good enough that when Intuit acquired Parsons last year, it incorporated much of Tax Edge into another Intuit program, J.K. Lasser's Your Income Tax. A second copycat program, Tax Saver from Novell, also uses code licensed from Parsons.

If there's any application suited for the CD-ROM format (other than games), it's tax programs. A CD-ROM's 600-megabyte-plus capacity can hold voluminous IRS regulations and independent tax guides. Regrettably, the '94 CD-ROM versions offer few improvements over disk-based editions. The notable exception: TurboTax Multimedia, which clearly put a lot of ef-

section of the IRS code or an easier-to-read guide by tax expert Mary Sprouse. Sprouse also appears, as does *Fortune* Editor-at-large Marshall Loeb, in video clips offering tax advice—although it's hard to fathom what value the clips offer over the text screens.

By comparison, the CD-ROM versions of TaxCut, Tax Edge, and Lasser offer few features—save for sometimes-insipid video clips—not found in the disk versions. Meca obviously realizes the shortcomings of the TaxCut CD-ROM because it is offering it at the same price as the disk version—and throwing in two additional programs, Personal Attorney and Mortgages, Insurance & More.

Programs That Can Make Tax Time Easier

PROGRAM / COST* / MAKER	FORMAT	SYSTEM REQUIREMENTS**	COMMENTS
TURBOTAX / \$42 Intuit	Windows, DOS, Macintosh, CD-ROM	4 MB RAM 15 MB HD	Easier to jump between interview and actual IRS forms; best CD-ROM version. <i>Number of states: 28.</i> ***
TAXCUT / \$40 Meca Software	Windows, DOS, Macintosh, CD-ROM	4 MB RAM 7 MB HD	Best hand-holding for novices; improvements include nifty "what if" worksheet and summary screen. <i>Number of states: 28.</i>
PERSONAL TAX EDGE / \$19 Parsons Technology	Windows, DOS, Macintosh, CD-ROM	2 MB RAM 10 MB HD	Nice financial calculators; provides state forms for all 43 states that have an income tax.
SIMPLY TAX / \$35 Computer Associates	Windows	4 MB RAM 10 MB HD	Clumsy interview format; includes tax tips from Ernst & Young tax guide. <i>Number of states: 20.</i>
J.K. LASSER / \$20 Intuit	Windows, DOS CD-ROM	2 MB RAM 11 MB HD	Clone of Parsons' Tax Edge, but with help screens drawn from popular J.K. Lasser tax guide. <i>Number of states: 43.</i>
TAXSAVER / \$21 Novell	Windows, DOS	2 MB RAM 10 MB HD	Virtual clone of Parsons' Tax Edge, but with Novell's "Coach" providing help. <i>Number of states: 43.</i>

* STREET PRICE FOR FEDERAL EDITIONS; STATE PROGRAMS COST \$19 TO \$25 EACH ** MINIMUM FOR WINDOWS VERSIONS IF AVAILABLE, OR DOS IF NOT. RAM IS RESIDENT ACCESS MEMORY, HD IS HARD-DISK SPACE *** FOR WINDOWS AND MACINTOSH. DOS VERSION HAS 45 STATES

that includes powerful interest and depreciation calculators, which may prove valuable after tax season ends. Tax Edge may also appeal to residents of smaller states, since it provides companion programs for all 43 states with an income tax—or 15 more than TurboTax and TaxCut. The state programs run another \$19 each, at least \$6 less than

fort into improving last year's disappointing product.

VIDEO CLIPS. This year, TurboTax Multimedia provides 5,000 links to IRS tax publications—far more than any rival. The new version, which sells for about \$10 more than the disk-based program, offers strong "hypertext" links that allow users to jump straight from the tax form to the relevant

Thanks to improvements in programs such as TurboTax and TaxCut, tax software now may help you save time over doing your taxes by hand—and reduce the math errors that can delay your return. And if a program helps you spot a deduction you might have otherwise overlooked, it would more than earn its keep.

Dean Foust

HOW TO DECIPHER THE LATEST CODE

Everyone's excited about the Republican push to cut taxes in 1995, but '94's tax bill is waiting to be paid. While 1994's tax changes were not as dramatic as 1993's, there are enough to keep you and your accountant busy until April.

Take high-income taxpayers—roughly those making more than \$115,000 for singles and \$140,000 for marrieds—who are still reeling from 1993's retroactive tax hike. Last year, they had the option to pay the difference between the old and new tax rates in installments over three years. This year, they face a double whammy: paying the second installment and the higher tax for 1994.

If you elected the installment plan in '93, you don't have to pay now, even though bills went out in mid-January. They're not due until Apr. 17. (This year, the Apr. 15 falls on a Saturday). But you must write a separate check and return it with that bill—don't add it to your 1994 return. You can apply any overpayments in withholding or estimated taxes for 1994 to the installment. But if you make a mistake, the 1996 installment gets accelerated into 1995, plus you may have to pay interest on the 1995 bill.

Other changes to heed at tax time:

■ **Charity.** You need a receipt for each charitable contribution of more than \$250. You don't send these in, but you must have them by Apr. 17. The receipts must state that you

received no goods or services in exchange for the gift. If you did get something, its value must be subtracted from your gift.

■ **Job change.** To get a write-off for moving to take a new job, the new workplace must be at least 50 miles farther from your old house than the old job was—up from 35 miles last year. So if your old job was 50 miles from your old

house, the new job must be 100 miles from your old house. You can no longer deduct the costs of hunting for the new house or selling the old house, or such expenses as meals associated with the move. Still, there are two silver linings: Employer's reimbursements of moving expenses won't be included as income on your W-2. And you no longer need to itemize moving expenses but can take them right off your income.

■ **Home financing.** Be-

fore interest rates went up, many people bought homes or refinanced mortgages in 1994. The good news is you can now deduct any points the seller paid for you. Although you can deduct points on a new home, if you refinanced, you must amortize points over the life of the loan. But those who refinanced for a second time can fully deduct points from the first refinancing.

■ **Social Security.** Social Security recipients will feel the

pinch this year, as the percentage of benefits that are taxed rises from 50% to 85% for those with income more than \$34,000 for singles or \$44,000 for married couples filing jointly.

■ **Business expenses.** Businesses, particularly service companies and people who are self-employed, face a cut from 80% to 50%, in the amount of meal and entertainment expenses they can deduct for business purposes. You can no longer write off social club dues at all.

Some Commonly Overlooked Deductions

- Financial periodicals used for investment advice
- Expenses for managing your investments, trustee fees for your IRAs if separately billed and paid
- Alcohol and drug treatment
- Business gifts of \$25 or less
- Union dues and gifts paid through payroll deductions to charities such as United Way
- Expenses related to job search, including counseling
- Self-employment tax
- Cellular phones and computers necessary for work
- Education that helps you in your job
- Alimony

Once again, Congress did not extend the provision allowing self-employed people to deduct 25% of their health insurance costs. But the government is expected to act retroactively this year. You might be able to get an extension on this is cleared up in May or July, says Tom Wenschlager, a partner at Grant Thornton. Or you can claim it and amend your return later. On the downside: Don't forget a few overlooked deductions. You can write off 50% of your self-employment tax.

Sole proprietors have until Apr. 17 to set up a self-employment pension (SEP) for their business if they miss the Dec. 31 deadline for opening a Keogh plan. You can sock away and deduct 12.5% of your annual net earnings with a SEP. If you have 28 employees or less, you can contribute pretax dollars from their salary to a salary-reduction simplified employee pension, or SARSEP, which is more complicated to administer. Contributions to Keoghs and SARSEPs made by Apr. 17 can be deducted from your taxes. And given the many small additions to this year's tax code, you'll need all the deductions you can muster. Pam



TAX PLANNING: BETTER NOT WAIT ON CONGRESS

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and then sell them to

lock in your profit. By holding a long and short position in a stock simultaneously, you cancel out any fluctuations if the price rises or falls, and you defer the sale until you repay the broker. But beware of the costs of employing these delaying strategies. "You have to look at how much gain you'll wind up with after you pay the trans-

do IRAs and 401(k)s, and they don't, that's sort of not forgiven in the world of tax planning," says Clinton Stretch, a partner at Deloitte & Touche. "Come September, when they finally get around to passing this bill, it may be too late to start saving, and that would be a permanently lost opportunity."

In any event, you should be maximizing contributions to tax-deferred retirement plans such as current IRAs and 401(k)s now. Don't wait: The sooner you put the money away, the sooner it starts compounding tax-free.

to a \$700 raise for those in the 15% bracket making up to \$38,000 a year. There isn't very much taxpayers can do to plan for such a break—just don't spend the money in anticipation of the tax break, in case it doesn't pass, cautions Stretch.

TRIED AND TRUE. Don't forget the old standbys, meanwhile. If you're in a high tax bracket and want to buy bonds, consider tax-free municipals. Contribute to flexible spending accounts offered through work that allow you to pay for medical and child-care expenses in pretax dollars. Shift income-producing assets to your children under 14 years

old: The first \$600 in unearned income is tax-free, and an additional \$600 would be taxed at only 15%. Anything more gets taxed at the parents' rate. If your kid is over 14, all his or her income will be taxed as an adult.

Make personal credit-card debt deductible by consolidating it with a home-equity loan. And make charitable gifts of appreciated stock or property, because you can write off the present market value without realizing the gain.

If you stick with these perennial strategies, any tax breaks that do manage to make it through the new Congress will be gravy down the line.

Pam Black



action fees," says Carl Duyck, a tax partner at Deloitte & Touche in Washington.

BE PREPARED. The GOP also would create a new back-loaded IRA. You wouldn't get a deduction for monies contributed to the account, but you could withdraw them tax-free at retirement.

The tax-free growth and withdrawal would provide a "tremendous benefit later on," says Tom Ochenschlager, a Washington partner at Grant Thornton. And both Republicans and Democrats are talking about loosening restrictions on IRAs so you could withdraw money without a penalty for expenses such as buying a home, paying for college, or certain medical bills.

One way to plan ahead is to have some cash on hand to put into a new, improved IRA. "If people are eligible to

There's also likely to be some kind of break for middle-class parents. The Republicans want a \$500 tax credit for each child under age 18 for parents with incomes up to \$200,000. The Democrats want \$300 per child under 13 for parents making up to \$100,000. Some version is likely to pass, says Stretch. This may not seem like much, but a \$500 tax credit is equal

WORTH NOTING

■ **WAR BONDS.** Many Series E war bonds issued in the 1940s and early '50s have reached their 40-year maturity and stopped earning interest, so cash them in. But be prepared for a tax blow, says Cleland Noret, a Modesto (Calif.) enrolled agent (licensed to represent individuals before the IRS). A bond purchased in 1954 for \$750 is worth more than \$7,000. The \$6,337 gain is taxable as ordinary income on federal returns.

■ **TAXING OPTIONS.** *Taxes & Investing: A Guide for the Individual Investor* covers tax rules on stocks, bonds, and options trades. The free 48-page booklet is offered by the New York Stock Exchange (800 692-6973).

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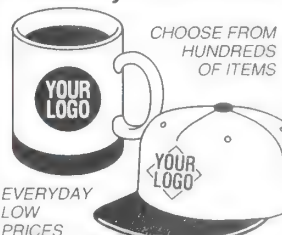
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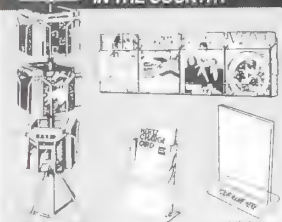
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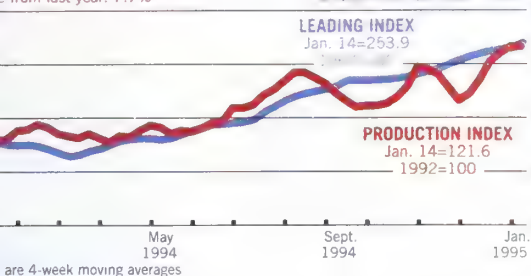


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Business Week Index

PRODUCTION AND LEADING INDEXES

Change from last week: 0.0%
Change from last year: 7.7%



Production index was unchanged during the week ended Jan. 14. Increases in seasonally adjusted output of electric power and lumber offset declines in autos and trucks. Before calculation of the four-week moving average, the index edged up to 121.4, from 121.

Leading index rose in the latest week, lifted by stronger growth in real estate. The unaveraged index also increased, to 256.2, from 253.5.

Source: index copyright 1994 by McGraw-Hill Inc.

BW leading index copyright 1994 by CIBC

FINANCIAL INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
PRICES (1/20) S&P 500	468.18	462.36	-1.3
RATE BOND YIELD, Aaa (1/20)	8.44%	8.46%	22.0
RIAL MATERIALS PRICES (1/20)	114.0	113.5r	NA*
SS FAILURES (1/13)	299	384	9.9
STATE LOANS (1/11) billions	\$462.6	\$459.8	10.3
SUPPLY, M2 (1/9) billions	\$3,571.8	\$3,570.9r	1.1
CLAIMS, UNEMPLOYMENT (1/7) thous.	354	338	-0.8

Source: Center for International Business Cycle Research (CIBC), Standard & Poor's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures companies), Federal Reserve, Labor Dept. CIBC seasonally adjusts data on failures and real estate loans. *Historical data available from CIBC.

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
L FUNDS (1/24)	5.45%	5.69%	2.97%
RGIAL PAPER (1/25) 3-month	6.26	6.09	3.15
ICATES OF DEPOSIT (1/25) 3-month	6.27	6.22	3.12
MORTGAGE (1/20) 30-year	9.25	9.35	7.14
ABLE MORTGAGE (1/20) one-year	6.90	6.88	4.24
(1/25)	8.50	8.50	6.00

Source: Federal Reserve, HSH Associates, Reuters Holdings PLC

Index in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

FINANCIAL INCOME

Jan. 30, 8:30 a.m. ▶ Personal income likely rose by 0.6% in December, up from 0.1% in November, according to a median forecast of economists polled by International, a unit of McGraw-Hill. Consumer spending probably increased 0.5% in December, half of the 0.6% gain in November.

LABOR COSTS

Jan. 31, 8:30 a.m. ▶ Wages and salaries for private workers likely grew 0.4% in the fourth quarter, up slightly from 0.3% in the third quarter. If so, labor costs in 1994 rose 3.1%, slower than the 3.5% increase in 1993.

CONSUMER CONFIDENCE

Tuesday, Jan. 31, 10 a.m. ▶ Consumer confidence probably slipped to 101.8 in January, says the MMS survey. In December, the confidence index was 102.2.

LEADING INDICATORS

Wednesday, Feb. 1, 8:30 a.m. ▶ The government's composite index of leading indicators likely rose just 0.1% in December, on top of a 0.3% advance in November.

NAPM SURVEY

Wednesday, Feb. 1, 10 a.m. ▶ The National Association of Purchasing Management's business index likely fell to 57% in January, from 57.5% in December.

CONSTRUCTION SPENDING

Wednesday, Feb. 1, 10 a.m. ▶ Building outlays probably rose 0.4% in December on top of a strong 0.7% gain in November.

NEW SINGLE-FAMILY HOME SALES

Thursday, Feb. 2, 10 a.m. ▶ Sales likely fell to a 680,000 annual rate in December. November sales slid 2.5% to 693,000.

EMPLOYMENT

Friday, Feb. 3, 8:30 a.m. ▶ The MMS survey calls for a 220,000 gain in nonfarm payrolls in January, just a bit slower than the 256,000 new jobs created in December. The January jobless rate is expected to be unchanged from December's 5.4%.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (1/21) thous. of net tons	1,991	2,035#	17.2
AUTOS (1/21) units	114,987	130,581r#	36.6
TRUCKS (1/21) units	92,365	102,933r#	42.5
ELECTRIC POWER (1/21) millions of kilowatt-hrs.	59,187	60,590#	-12.6
CRUDE-OIL REFINING (1/21) thous. of bbl./day	13,553	13,847#	2.0
COAL (1/14) thous. of net tons	21,731#	17,702	10.3
PAPERBOARD (1/14) thous. of tons	NA	NA	NA
PAPER (1/14) thous. of tons	NA	NA	NA
LUMBER (1/14) millions of ft.	464.6#	364.5	-7.1
RAIL FREIGHT (1/14) billions of ton-miles	24.2#	19.5	8.5

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPAA, SFPA, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (1/25) \$/troy oz.	381.450	382.600	-0.7
STEEL SCRAP (1/24) #1 heavy, \$/ton	147.00	147.00	5.4
COPPER (1/21) ¢/lb.	145.5	144.0	62.0
ALUMINUM (1/21) ¢/lb.	100.5	98.0	73.3
COTTON (1/21) strict low middling 1-1/16 in., ¢/lb.	88.44	87.34	34.3
OIL (1/24) \$/bbl.	18.66	18.35	20.8

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (1/25)	99.71	99.52	109.16
GERMAN MARK (1/25)	1.52	1.53	1.73
BRITISH POUND (1/25)	1.59	1.57	1.50
FRENCH FRANC (1/25)	5.26	5.29	5.90
ITALIAN LIRA (1/25)	1599.0	1616.5	1695.3
CANADIAN DOLLAR (1/25)	1.42	1.42	1.32
MEXICAN PESO (1/25) ³	5.755	5.300	3.104

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

Fidelity Investment Challenge



LEADERS

Update #4 • Closing Values as of 1/19/95

Participants in the Fidelity Investment Challenge. On November 14, over 3,500 amateur investors began trading with a fictional \$250,000 portfolio. Over the course of the next 3 months, they will buy, sell, or short any stock listed on the NYSE, AMEX, or OTC.

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Rank	Investor	City, State	Equity Value
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2	David Evansen	Boca Raton, FL	\$428,559
3	Jim Jacobsen	Somerset, KY	\$418,995
3	Gregory Spencer	Sarasota, FL	\$394,500
4	Mike Gilledder	Morristown, NJ	\$382,072
5	Ron Tamlyn	Dallas, TX	\$377,750
6	Henry Sodke	Austin, TX	\$373,320
7	George Mergenov	Longwood, FL	\$372,490
8	William Miller	Murfreesboro, TN	\$367,973
9	Richard Barron	Rockville, MD	\$365,667
10	Charles Lechialo	West Newton, MA	\$363,284
11	Eric Baird	New York, NY	\$358,650
12	Yitzhak Peykar	Brooklyn, NY	\$357,446
13	Jamie Weiss	Portsmouth, NH	\$353,890
14	Steven Butler	Ronkonkoma, NY	\$351,450
15	Phillip Zagran	Stuart, FL	\$342,338
16	Donald Johnson	Pittsford, NJ	\$342,137
17	Anatoly Raklyar	Brooklyn, NY	\$341,470
18	Robin Ashworth	Covington, KY	\$340,949
19	Dwayne Hallman	Houston, TX	\$338,582
20	Robert Kratz	New Hyde Park, NY	\$337,539
21	David Bradley	Asheville, NC	\$337,326
22	Scott Motter	Bethlehem, PA	\$336,697
23	Subash Gajenbragadjar	Beckley, WV	\$334,699
24	Michael Serezo	Augusta, GA	\$333,698
25	Shirley Lyter	Seattle, WA	\$332,946
26	Michael Wood	Shawnee Mission, KS	\$329,369
27	Terry Hall	Burlington, MA	\$328,965
28	Dennis Hansen	Pittsburgh, PA	\$328,607
29	A. Robert Lawton	Wexford, PA	\$328,089
30	Kim Brust	Porter Corners, NY	\$328,060

THE COMPETITION UP CLOSE

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Portfolio Value of the 100th Ranked Account	\$297,739

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Index to Companies

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A

ABB Group 62, 149
Activision 143
AIM Aggressive Growth 108
AlliedSignal 34
Alcoa 144
America Online 70
AMG Data Services 108
Amgen 150
Amoco 164
Amtrak 62
Apple 20
AT&T 4, 146, 147, 149, 152
Aviation Data Service 66
Aviation Methods 66

B

Bandai 143
Bank of Japan 55
Barclays de Zoete Wedd 55
Baring Securities 55
Bausch & Lomb 45
Bell Atlantic 44, 147
Bellcorp 6
BellSouth 147
BMW 66
Boeing 62
Bombardier 62, 66
Brio Industries 143
Bristol-Myers Squibb 149, 150
Brown & Williamson Tobacco 6

C

Cadus Pharmaceutical 149
Canadair 62
Caradco 144
Caremark International 42
Caterpillar 37
Cazenove 56
CCI Asia-Pacific 52
Cemex 32
Chevron 143
Chrysler 37, 66, 143, 144
Claritas 20
CNBC 42
Coca-Cola 4, 42, 44, 143
Compaq Computer 20, 32, 38
CompuServe 70
Computer Associates International 154
Concarri 62
Corridor Broadcasting 49
Crabbe Huson Equity 108
Crabbe Huson Special 108
Credit Capital Finance 32
CSX 34

D

Dassault 66
Dataquest 149
Deere 37
Dell Computer 36
Deloitte & Touche 157

Disney 66

DRI/McGraw-Hill 28, 36, 60
Duff & Phelps 56
Dun & Bradstreet 28

E

Electrosources 143
Epitope 42
Ericsom (L.M.) 152
Electricité de France 149

F

Fidelity Asset Manager 108
Fidelity Blue Chip Growth 108
Fidelity Capital Appreciation 108
Fidelity Investments 45, 52
Fidelity Magellan 108
First Team Sports 143
Flex-funds Muirfield 108
Ford Motor 37, 143
Forstmann Little 66
Founders Worldwide Growth 108
Frank Music 70

G

Gateway Index 108
GE 34, 52, 66
GEC-Alsthom 62
Glaxo 56
GMO 143
Goldman Sachs 52, 56
Govett 56
Grant Thornton 156, 157
Greyhound 45
Growth & Income 108
GT Global 32
GTE 147
Gulfstream Aerospace 66

H

Hambros 56
Hancock Special Equities 108
H&R Block 154
Hanover Sterling 42
Harley-Davidson 108
Heartland Biotechnologies 149
Honda 37
Honeywell 6, 66
Howard Services 12
HPI Beverages 143
HSBC Investment Banking 56

I

IBM 32, 149
Immunex 150
Indigo 44
I/Net 20
Interactive Cable Systems 147
Intuit 154

J

James Capel Pacific 32
JB Food Industries 143
J.B. Hunt Transport 144

J.P. Morgan Securities 150
J.W. Charles 143

K

Kemper Financial Services 32
Kidder, Peabody & Co. 42
KnowledgeWare 45

L

Lazard Brothers 56
LCI International 146
Learjet 62
Levesque Beaubien Geoffron 62
LEXIS Counsel Connect 70
Lindner Dividend 108
Lipper Analytical 108
Los Angeles Rams 45
Los Angeles Times 35
Lotus 45
Lufthansa 62

M

Mabon Securities 146
Macromedia 143
MapInfo 20
Marquardt Switches 12
McFarland Energy 143
McGraw-Hill 161
MCI Communications 147
Meca Software 154
Merger Funds 108
Merrill Lynch 32
Merrill Lynch Global Allocation B Fund 108
Merrill Lynch Japan 55
Microsoft 20, 45
Mitsubishi 55, 66
Montgomery Asset Management 32
Moody's Japan 55
Moore 44
Morgan Grenfell 56
Morgan Guaranty Trust 32
Morgan Stanley 32, 56
Morningstar 108
Morningstar Mutual Funds 108
Motorola 143, 152
M.R. Weiser 157

N

Nashville Banner Publishing 45
NationBank 56
NEC 55
Neuberger & Berman Focus 108
Neurobiological Technologies 143
Nextel Communications 147
Nokia 152
North Star Steel 36
Novell 154
Nynex 146, 152

O

Odwalla 143
Oki 152
Oneac 12
Oregon Steel Mills 36

P

Pacific Telesis 147
PaineWebber 36
Panmure Gordon 56

PBHG Growth 108
Philip Morris 6
Philips 45
Phoenix Management Plantronics 152
Pocket Books 6
Prodigy Services 70

Q

Quaker Oats 42, 146

R

Rantoul Products 14
Robert Fleming 56
Robertson Stephens Contrarian 108
Rolls-Royce 66

S

Salomon Brothers 32
Sanford C. Bernstein Savi Technology 149
Schroders 56
Scripps Research Institute 149
Seagram 66
Seligman Communications & Information 108
S.G. Warburg Group Short Brothers 62
SI Diamond 6
Siemens 62
SIG 149
Sill-Terhar Ford 37
SkyWest 62
Smith Barney 32
Smith New Court 56
Snapple 143
Sogen International Solarmax 143
Sony 45
Sound Waves 152
Starbucks 45
STB Systems 20
Strategic Insight 108
Stratton Oakmont 70
Suarez Corporation Industries 70
Sumeria 20

T

Teléfonos de México 2
Time Warner 45
Toshiba 45
Toyota 55
T. Rowe Price New Horizons 108
Trust Group 4
Twentieth Century Group Investors 108

U

Union Bank of Switzerland 56
United Airlines 144, 146
United New Concepts U.S. Electricar 143

V

Van Kasper 143
Vical 150

W

Walt Disney 62
Warburg Pincus Growth Income 108
WCI Steel 36
Wellcome 56
Wharf (Holdings) 52
Wheelabrator 49
Windmere 52
Wing Group 52

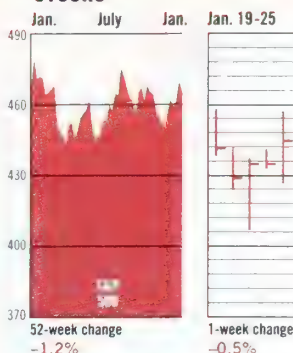
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Investment Figures of the Week

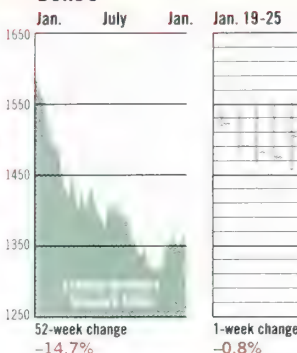
MARKET ANALYSIS

Markets are rising, currencies are falling, and the stock markets are mixed. The Dow industrials rose 15 points in a row before making a gain on Jan. 25 and finishing down 1.5%. The U.S. market is a reflection of strength. The British market is down over 2%, the German market is up over 3%. South of the border, the Mexican stock market continued to lose ground. The Nikkei dropped 5.5%, as investors assessed the financial damage from the Kobe earthquake.

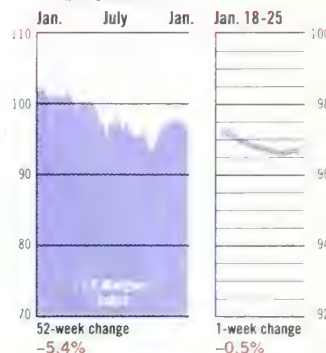
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS

	Latest	% change	
		Week	52-week
DOW INDUSTRIALS	3871.5	-1.5	-0.9
COMPANIES (S&P MidCap Index)	171.5	-1.2	-4.2
COMPANIES (Russell 2000)	248.8	-1.4	-5.3
COMPANIES (Russell 3000)	267.5	-0.7	-2.1
	Latest	% change (local currency)	
		Week	52-week
FINANCIAL TIMES 100	2982.2	-2.4	-13.2
Nikkei Index	18,159.5	-5.5	-5.1
FTSE COMPOSITE	4106.4	-1.5	-7.9

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.93%	5.85%	2.98%
30-YEAR TREASURY BOND YIELD	7.86%	7.77%	6.31%
S&P 500 DIVIDEND YIELD	2.77%	2.76%	2.57%
S&P 500 PRICE/EARNINGS RATIO	16.6	17.1	22.5

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 200-day moving average	458.4	457.9	Positive
Stocks above 200-day moving average	37.0%	40.0%	Positive
Speculative sentiment: Put/call ratio	0.64	0.53 r	Neutral
Insider sentiment: Vickers sell/buy ratio	0.88	0.94	Positive

BLOOMBERG FINANCIAL MARKETS

INDUSTRY GROUPS

WEEK LEADERS

	% change	
	4-week	52-week
SEMI-CONDUCTORS	9.4	15.2
TELECOMS	9.1	-26.0
FREE TIME	9.0	-4.6
MARKET AUTO PARTS	6.8	-11.8
GLASS CONTAINERS	6.4	6.5

Strongest stock in group

	% change		Price
	4-week	52-week	
ADVANCED MICRO DEVICES	36.6	62.3	31 1/4
USAIR GROUP	11.8	-67.5	4 3/4
BALLY ENTERTAINMENT	23.1	-15.8	8
ECHLIN	12.9	1.1	33 7/8
BALL	9.5	19.8	33 1/4

WEEK LAGGARDS

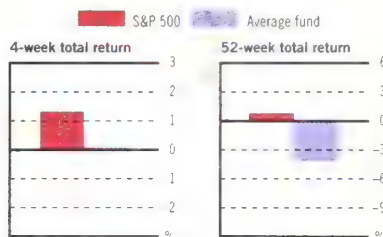
	% change	
	4-week	52-week
TELECOMS	-4.9	-28.0
TELECOMS	-3.7	18.4
DISTANCE TELECOMMUNICATIONS	-3.6	-17.0
TELECOMS	-3.6	-17.5
TELECOMS	-3.2	19.1

Weakest stock in group

	% change		Price
	4-week	52-week	
GENERAL MOTORS	-6.1	-36.3	38 3/4
STRIDE RITE	-7.5	-38.6	10 3/4
AT&T	-4.7	-13.2	48 5/8
ROADWAY SERVICES	-7.7	-20.1	50 3/4
AVON PRODUCTS	-6.8	5.3	56 7/8

MUTUAL FUNDS

	%	LAGGARD'S	%
4-week total return		Four-week total return	
WRIGHT EQUIFUND-MEXICO NATL. FID. EQTY.	7.2	WRIGHT EQUIFUND-MEXICO NATL. FID. EQTY.	-23.5
BT INVESTMENT LATIN AMERICAN EQUITY	6.8	BT INVESTMENT LATIN AMERICAN EQUITY	-16.7
HERCULES LATIN AMERICAN VALUE	6.5	HERCULES LATIN AMERICAN VALUE	-15.6
52-week total return		52-week total return	
MONITREND GOLD	30.7	MONITREND GOLD	-55.0
STEADMAN OCEANOGRAPHIC TECHNOLOGY	25.1	STEADMAN OCEANOGRAPHIC TECHNOLOGY	-40.2
WRIGHT EQUIFUND-HONG KONG NATL. FID. EQ.	24.4	WRIGHT EQUIFUND-HONG KONG NATL. FID. EQ.	-40.1



RELATIVE PORTFOLIOS

Relative portfolios represent the value of \$10,000 one year ago. Relative portfolios indicate total returns.

Money market fund
\$10,491
+0.28%

U.S. stocks
\$10,086
-0.89%

Gold
\$10,081
+0.39%

Foreign stocks
\$9,875
-4.16%

Treasury bonds
\$8,724
-1.60%

This page is as of market close Wednesday, Jan. 25, 1995, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are

as of market close Jan. 24. Mutual fund returns are as of Jan. 20. Relative portfolios are valued as of Jan. 24. A more detailed explanation of this page is available on request. r=revised

HELPING MEXICO IS SELF-HELP

Who lost Mexico and triggered the capital panic of '95? If Republicans and Democrats aren't careful, people will soon start blaming Congress, thanks to continued bickering over the Administration's \$40 billion bailout of Mexico.

Take a look around the world. Equity, bond, and currency markets are jittery. A serious capital flight to quality is already under way. The Kobe earthquake and the impending death of Chinese leader Deng Xiaoping have Asia on edge. Argentina and Brazil are holding their breath over the peso crisis. Europe is split between a strong Germany and everybody else. The Russian ruble is at an all-time low. America must show leadership at this critical period—and fast—or a world liquidity crisis could trigger a recession.

Not that Washington should give a blank check to the Mexicans. Far from it. In exchange for the loan guarantee, the U.S. should insist on major reforms. Economic liberalization has so far helped the biggest Mexican conglomerates and U.S. multinationals investing in Mexico, but small and medium-size companies remain stuck. As a consequence, economic growth has been anemic, with weak job creation.

To change that, three things are needed. First, Mexico should cut its high tax rates. Lowering its 10% value-added tax would be a start. Even better for small-business owners would be raising the level at which taxes begin to be withheld. Withholding currently starts at \$5,000. It should be boosted significantly. Declaring a three-year tax holiday for new small-business investments alone might generate half a million jobs a year. Revenues lost to the government can be made up by selling off state-owned companies and banks.

Second, Mexico has to raise its savings rate so that it no

longer depends on the kind of private foreign-capital investments that have proved to be so "hot." Mutual-fund money, in particular, has shown itself to be skittish in the face of higher perceived risk. The Asian nations are financing their growth with a mix of internal savings and foreign funding. Mexico must begin to reward private savings, too, perhaps like Chile.

Finally, Mexico's central bank must become more transparent. Official dissembling about dwindling dollar reserves was a key factor in the peso meltdown. Had the markets seen the decline, they would have forced the government to act before the retreat became a rout. GOP leader Bob Dole is pushing a notion of an Argentine-style currency board. Mexican nationalism would make that difficult. Nevertheless, that doesn't mean that its central bank can't publish its reserves on a timely basis.

There is plenty of blame to go around over the peso. Former President Carlos Salinas de Gortari should have let the peso fall more sharply in the last months of his presidency. The monetary printing presses rolled to help the election of Ernesto Zedillo Ponce de León. The Clinton Administration, particularly the Treasury, fumbled the ball on financial aid.

But Congress must keep its eye on what is really at stake. Mexico is in the middle of a serious political and economic evolution that is bringing true democracy and free markets to nearly 100 million people for the first time in their history. There are many old-style politicians and union bosses tied to the state sector who would be only too happy to see Mexico turn protectionist once again. It is in the national interest of the United States to deny them victory and support the forces of change.

THE TRADE DEFICIT: THERE'S A BRIGHT SIDE

What a difference seven years makes. The last time the U.S. ran a \$170 billion trade deficit, back in 1987, there were dire warnings of "hollowing out" the country's manufacturing sector, importing higher inflation, and going into hock to foreign—especially Japanese—creditors. Remember the hue and cry about becoming a nation of hamburger flippers dependent on the kindness of strangers?

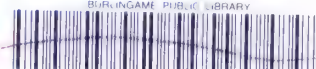
This time around, the U.S. is importing relatively more capital equipment, rather than consumer goods, thus helping to boost U.S. productivity and competitiveness. In fact, capital goods are the fastest-growing category of imports, up 21% over last year vs. 9% for consumer items (page 36).

This has helped make the U.S. No. 1 again in productivity. Its factories are producing flat out to satisfy both local and export markets—with the exception of Detroit, which may be pricing its cars too high. Overall, imports are not grabbing market share, they are satisfying the overflow of demand that local capacity can't meet. That keeps a lid on inflation.

Another major change is in the sourcing of imports. Between 1980 and 1987, Japan, Western Europe, and the Asian tigers accounted for 75% of growth in U.S. imports. But by last year, flows had shifted so that Canada, China, and Mexico provide 68% of all import growth. The stimulus to economic growth provided by the trade deficits has shifted dramatically back to North America—plus China.

Barring a foolish rejection by Congress of the Mexico package, there is no reason to fear higher U.S. imports from its North American neighbors. Where free markets reign, higher imports will lead to higher exports because they generate new incomes and greater demand for U.S. goods.

The real problem in U.S. trade continues to lie in markets where foreign goods do not have equal access. The chronic deficit with Japan is no less irksome for being an old story—a tale that is showing signs of recurring with China. Heretofore, serious work in opening up markets to U.S. exports remains to be done.



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BusinessWeek

JANUARY 13, 1995

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CEO OF HEWLETT-
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HP 17" Color Display
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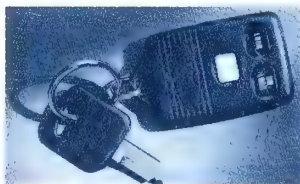
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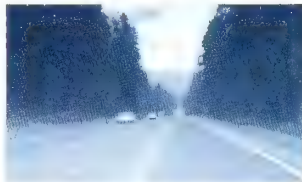
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SHARING THE HERITAGE OF BEING NUMBER ONE.

BusinessWeek

FEBRUARY 13, 1995

COVER STORY

Southwest Airlines is one of the scrappiest big companies in America, and Rita Bailey is part of the reason why

page 64



Cover Story

64 GO-GO GOLIATHS

Behemoths such as Motorola and VF are proving that big doesn't always mean bumbling. They're among the huge companies racking up growth rates in sales and profits far ahead of their peers—and giving the lie to knee-jerk naysaying about giant U.S. corporations

65 HOME DEPOT'S BATTLE PLAN

How it assaults and holds new territory

67 HEWLETT-PACKARD'S SPEEDUP

A rapid-fire delivery of new products

69 SOUTHWEST'S PICKY PEOPLE DEPT.

The importance of personnel choices

70 NUCOR'S INDEPENDENT SPIRIT

Plant managers call their own shots

News: Analysis & Commentary

32 CLINTON'S NEW DEAL FOR MEXICO

The \$50 billion aid package is a big step toward creating a global safety net to insure against market panics

35 COMMENTARY

If Clinton and Congress can't come to terms on Mexico...

36 MEXICO MAY STILL NEED CPR

Financial rescue or not, Zedillo faces widespread economic pain and a rocky political road to recovery

38 COMMENTARY

With its billions of risk spread among so many partners, Clinton's Mexico bailout reflects the New World Order of finance

40 HALFWAY UP THE HILL AT GM

A solid fourth quarter for American operations does not a turnaround make

44 COMMENTARY

It's time to give the hook to Lane Kirkland's outdated act at the AFL-CIO

46 FIDELITY'S CONTRACT WITH AMERICA

The ouster of bond-fund head Tom Steffanci signals a conservative shift

48 THE PEACOCK STRUTS ITS STUFF

NBC still has a way to go, but it's scoring notable ratings victories

48 THIS GADFLY IS REALLY BUZZING

Calpers is issuing fresh reprimands to laggard boards

50 IN BUSINESS THIS WEEK

Union Pacific, Marion Merrell Dow, Denver's airport, L.A. Gear, cancer consortium, Howard Stern, cyberspies

International Business

54 GERMANY

The telecom market is opening, Deutsche Telekom's rivals are reeling

55 GERMANY

Tough union demands could jeopardize the country's fragile recovery

56 JAPAN

Sumitomo's \$8 billion write-off signals that Japan's banks may be facing a crisis

60 HONG KONG

Even for real estate, what goes up must come down

61 INTERNATIONAL OUTLOOK

Israel: Will staring into the abyss bring peace back on track?

Economic Analysis

24 ECONOMIC VIEWPOINT

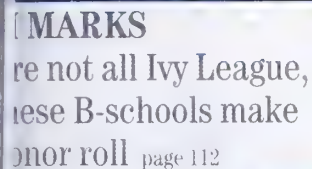
Dornbusch: The middle class's stock market

28 ECONOMIC TRENDS

Detroit's long-term worries, bosses' stakes in their companies, the upsurge in rising rates, global merger mania

29 BUSINESS OUTLOOK

Maybe now the Fed will lay off the



Put materials under
awesome pressure—and
watch the alchemy **page 76**

After a year of unmitigated disaster, bonds are starting to look tempting again

page 94

Clinton cobbled
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The CBOT's Pat Arbor and the Merc's Jack Sandner slug it out in the pits **page 62**

page 62

rinking the rule book for business

le chairmen of Chicago's two
changes just can't get along

With sales suddenly going flat, Chrysler and Ford are back to their old tricks

ENNZOIL TURNS ON A SEARCHLIGHT

fewer deals, more oil and gas hunts

Research in high pressure is yielding substances with exotic qualities

Waste silicon, supercomputers the little
guys can borrow, green companies'
economic edge, pills that alert the user

Even in today's sophisticated, information-rich environment, markets are ruled by herd instincts

Precedent suggests that Orange County has a strong case against the broker

GTech and Intl. Game Technology
A saucy target in Heinz
Is Bristol-Myers stalking Amgen?

At last, Apple has a Macintosh that really does Windows

It's losing ground in the online-service sweepstakes. But an overhaul, including a new system, could save it

American and homegrown services are betting that this is the year the Continent goes online en masse

They're showing signs of life—and BUSINESS WEEK's rankings will help you spot the likeliest of the bunch.

"Duration" is a guide to riskiness

SMART MONEY: In search of sexier CDs

Ness and Williams: *Why We Get Sick*
 Frankel: *Beyond the Promised Land*
 Heilbroner: *Visions of the Future*
 Auchincloss: *The Collected Stories of Louis Auchincloss*

118 EDITORIALS

Up Front

EDITED BY LARRY LIGHT WITH RUTH COXETER

LOOPHOLES

HOW BIG OIL DEFIES THE GREAT SATAN

PURCHASES OF IRANIAN OIL by U.S. companies are becoming a political sore point. Reason: They undercut the Clinton Administration's current campaign to get Europe and Japan to curb trade and financial aid to Tehran.

The U.S. has banned imports of Iranian crude oil since 1987 when the Iranians attacked U.S.-flagged tank-



END RUN: Iranian oil gets through

ers in the Persian Gulf. But there's a loophole. U.S. oil giants can buy and sell Iranian crude through overseas subsidiaries. Oil industry analysts say these subs take 20% to 30% of the 2.5 million barrels daily that Iran exports, enriching Tehran's cof-

fers by up to \$4 billion yearly. Exxon is Iran's single biggest customer. A company official confirms that Exxon buys 250,000 to 300,000 barrels per day from Iran for refineries in Europe and Asia.

This alarms the People's Mojahedin of Iran, the foremost resistance group to the Tehran regime. It says the sales effectively subsidize terrorism and repression.

Efforts are afoot to tighten the embargo. Senator Alfonse D'Amato (R-N. Y.) has just introduced a bill that

would bar U.S. companies from overseas purchases of Iranian oil.

That's not likely to work, as the oil producers point out. Surging world demand for oil means that, with a tighter embargo, Iran will simply sell more to other cus-

tomers. So Tehran's treasury wouldn't be dented, but the Saudi and Kuwaiti oil that U.S. buyers would have to shift to would be more costly. And Europeans would howl at any U.S. attempt to extend its jurisdiction abroad. *Amy Borrus*

DEFAULT LINE

ORANGE COUNTY'S FLACK FLAP

BUFFING UP A TATTERED image ain't cheap. Especially if you're running bankrupt Orange County. The Board of Supervisors got billed \$238,000 for December's last three weeks by Sitrick & Co., a Los Angeles public-relations firm specializing in financially ailing outfits (other clients include America West and Greyhound). Nor will January's bill be small.

Worth it? Michael Sitrick says his firm managed to kill some negative news stories

and mute others. His biggest coup may be casting most of the blame on departed county Treasurer Robert Citron. Sitrick, who is accused by a newly elected supervisor of overcharging, argues he is cheaper than other nationally known spinmeisters.

Meanwhile, libraries are closing early, and schools may have to. Sitrick's hefty fee is roughly what the county cut from health care for the poor to help meet debt payments. *Ronald Grover*

TALK SHOW "Slower growth is coming to a theater near you."

—Anthony Chan, chief economist of Banc One Investor Advisors, on the state of the U.S. economy

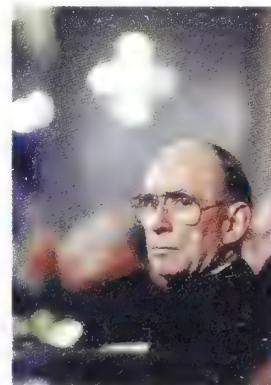
SETTLING UP

BLACK CASSOCKS AND RED INK

SEX-ABUSE COSTS ARE A growing burden for the U.S. Catholic Church. They pushed the Archdiocese of Chicago, for instance, into a \$1.5 million deficit last year. Priests' sexual misconduct cost the nation's second-largest archdiocese \$4.3 million in the fiscal year ended June, 1994—up 54% from \$2.8 million in 1993.

These cases are certainly hurting the Church everywhere, from Los Angeles, the largest archdiocese, to Santa Fe, N. M. In Chicago, where fiscal reports are among the most detailed, 65% of sex-case costs go to legal claims and settlements.

The situation in Chicago drew special attention a year when Joseph Louis Cardinal Bernardin himself was the target of a sex-abuse complaint. The archbishop dropped the charges, admitting that his memories had been wrong. The good news: 1994 may be the peak year



BERNARDIN: Cleared

because the Archdiocese started programs to deal with the problem.

The increasing sex-case expense in Chicago comes at a bad time. The Archdiocese fought chronic deficits for most of the past 10 years. When 1994's is down from a high

\$14 million in 1990—Chicago Church officials worry rising expenses are outpacing revenue so fast that a fiscal crisis looms within a few years. *Kevin K...*

THE LIST LOBBYIST PAYCHECKS

Heading an industry trade group is a wallet-friendly endeavor, especially for ex-government officials. Examples: LBJ aide Jack Valenti and former Senator Richard Schweiker. The best-heeled tend



POINT MAN VALENTI

to work for finance and communication groups, both facing intense regulatory action in recent years. Five years ago the highest-paid association honchos came from a wider array of industries.

10 BEST-PAID TRADE GROUP CHIEFS**

JACK VALENTI	Motion Picture Assn.	\$858,86
THOMAS ASHLEY***	Association of Bank Holding Companies	810,49
JASON BERMAN	Recording Industry Association of America	769,80
ROBERT VAGLEY	American Insurance Assn.	724,63
EDWIN HARPER	Association of American Railroads	712,78
RICHARD SCHWEIKER	American Council of Life Insurance	680,40
THOMAS WHEELER	Cellular Telecommunications Industry Assn.	650,00
RICHARD DAVIDSON	American Hospital Assn.	602,64
FRANKLIN NUTTER	Reinsurance Assn.	600,80
CATHLEEN BLACK	Newspaper Assn.	600,00

*Includes deferred compensation **Excluding benefits and allowances, as reported to Internal Revenue Service, for 1993 ***No longer employed here. DATA: NATIONAL JOURNAL



Meet the Face

Up Front

I-WAY PATROL

THE ONLINE AND THE RESTLESS

A SOAP OPERA ONLINE—IT had to happen. America Online subscribers will be able to read the weekly *Parallel Lives* this spring when it starts a three-month trial run. The 1,100-word episodes have illustrations and conclude with cliffhangers that are intended to lure people

Parallel Lives

NEW SOAPS: *Internet bound*

to tune in the following week.

The series has three separate story lines running simultaneously. According to its promotional material, a story called "One Point Seven" follows the Higgins clan, an

"un-sitcom" middle-class African American family living in postquake Los Angeles. In "Urban Studies," upscale Manhattanites go through nights of "sushi, samba lessons, and secrets." And "A Boy and His Dog" is set in a small town "where unseen dangers belie the sense of safety that hometown America once provided."

The cyber-soap is sponsored by Nabisco and served up—curiously—by the staid *New York Times* on its AOL service, @times. It will run alongside regular *Times* articles and arts reviews. The paper hopes readers will contribute online reactions to the family and social issues raised. *Edward C. Baig*

AFTERLIVES

A JUNK-FOOD JOHNNY APPLESEED

DONALD KENDALL, RETIRED as PepsiCo chairman since 1986, just can't stay away from the fast food. Kendall, 73, still devotes part of his time to expanding PepsiCo's fast-food empire—which includes Pizza Hut, Taco Bell, and Kentucky Fried Chicken—in the former Soviet bloc

and other emerging markets. Recently, Kendall flew to Poland to help his son, Donald Jr., who runs a chain of PepsiCo franchises there.



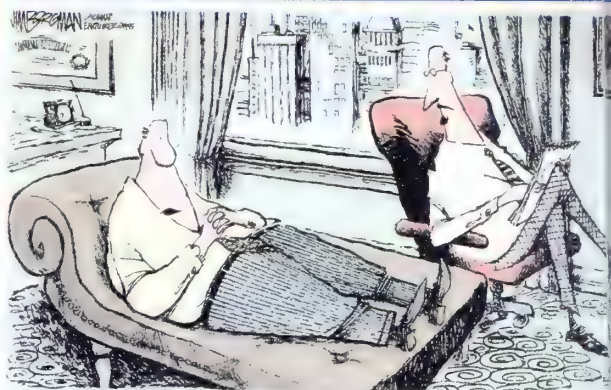
KENDALL:
Big names

That's not all. Kendall is the chairman of a new international investment fund that aims to take minority stakes in franchises. Launched Jan. 27, the Emerging Markets Franchise Acceleration Fund is managed by former Reagan Administration Treasury Deputy Secretary R. T. "Tim"

McNamar. Another big name, ex-Treasury Secretary Donald Regan, heads the fund's advisory board.

The fund plans to raise \$100 million initially, targeting franchises in PepsiCo and others, both food (McDonald's) and nonfood (Blockbuster Videos). PepsiCo, says Kendall, is "pretty excited about it." He also spends his time running two cattle ranches in Wyoming, heading the National Forest Foundation conservation group, and co-owning a New Orleans brewery pub with Donald Jr. and two other sons. *Phillip L. Zweig*

DRAWN & QUARTERED



"I'M A MIDDLE-CLASS WHITE GUY AND I'M JUST NOT PARTICULARLY ANGRY..."

OVER THERE

MICKEY GOES TO CHARM SCHOOL

DO MICKEY'S EUROPEAN helpers need hospitality lessons? Struggling Euro Disney is thinking about starting a special program next year to vet possible new hires for the entertainment complex outside Paris. Trainees would spend 6 to 12 months studying such things as how to please customers. Now, workers at Euro Disney and the two U.S. Disney parks get a single day's training, although they also participate in training seminars periodically.



CHEESE! That's how to smile

Walt Disney Co. figures that a school with a dorm would lure students from around Europe, making it

easier to reduce the staff's 65% French makeup. Some 55% of the park's visitors are non-French. And Disney might make a buck teaching other European companies employees Walt's ways.

Euro Disney insists it has no service problems, despite customer complaints that

it doesn't answer the phones. There has been friction with employees who balked at the squeaky-clean Disney culture. The union won a court battle forcing the park to back off its appearance code, which requires men to shave their beards and women to wear demure hairstyles. Even after a 1994 financial

restructuring, the park needs help. Attendance in the year ending Sept. 30 fell 1% and was 25% below the original plan. *Stewart J.*

THE BIG PICTURE

THE GLOBAL DEAL MILL

The U.S. is still the deal capital of the world. Despite a weak dollar last year, U.S. companies bought almost twice as many foreign outfits as foreigners bought in America. Cross-border deals in 1994 jumped 46%, to \$239 billion, up from \$163 billion the year before.

NUMBER OF DEALS, 1994		
HEADQUARTERS OF COMPANIES	BUYING FOREIGN COMPANIES	SELLING TO FOREIGN COMPANIES
U.S.	1,173	668
BRITAIN	644	435
GERMANY	434	350
FRANCE	350	317
JAPAN	336	85

DATA: KPMG PEAT MARWICK

FOOTNOTES Asked to rate service (0-100), consumers gave rental-car clerks highest marks, 91; grocery clerks lowest, 15



Meet the Face of the Future Today!

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Readers Report

MAYBE BIG GOVERNMENT JUST NEEDS FINE-TUNING

Robert Kuttner's column ("Rewrite the regulatory rulebook—don't tear it up," Economic Viewpoint, Jan. 23) illustrates that government regulation can be circumspect and creative. Too often, our bureaucracy fails to develop adaptable, responsive, and market-sensitive rules. Instead, what U.S. businesses end up confronting are one-size-fits-all mandates that are the product of agencies that don't consider the costs of regulation along with the supposed benefits.

Bruce A. Gates
Chairman

Project Relief
Falls Church, Va.

Editor's note: Project Relief is a coalition of businesses, think tanks, and individuals interested in regulatory reform. Gates also serves as vice-president for public affairs of the National-American Wholesale Grocers' Assn.

SOME PC BUYERS WANT TO SHOW GATEWAY THE DOOR

Perhaps the mail-order houses are capturing the market ("The computer is in the mail (really)," Information Processing, Jan. 23). But if they're not careful, they're going to lose it just as fast. Over the past five years, our company purchased numerous packages from Gateway.

We were impressed with the quality and value of the units, and early on we encouraged business associates and suppliers to look at the advantages of mail-order computers. Our views are changing.

Our latest unit came equipped with an extra-large, very expensive monitor. From the beginning, it was problematic, and its soul has finally gone to the big digital warehouse in the sky. We followed procedure by calling Gateway's tech service.

We made half a dozen calls daily and got: "We're busy and can't take your call. Try calling later." I faxed Gateway and pleaded for a human being to

respond. That was three weeks later. We've been without a functioning monitor for a total of five weeks with no response and no hope of resolving the problem.

R. Denny H.
Chief Operating Officer
Centerton Nursery
Bridgeton,

Last year, the monitor of a system Gateway 2000 I'd just bought blew down. It took me more than six months and more than 20 faxes to get my money back. Sure, a mail-order company has some virtues. But its corporate system is as primitive as mom-and-pop stores.

Nobuyuki
Higashiosaka, Japan

Editor's note: Gateway says these complaints are remnants of an unanticipated increase in demand and the structure of the customer-service department. It says it has already increased by 50% the number of calls it can take and will increase it by another 50% the next two months.

WHAT'S NEXT, 'THE HEAD-ON'?

Regarding "Shocker at GM: People like the Impact" (News: Analysis/Commentary, Jan. 23): To me, the shocker at GM is that someone would actually name a car "Impact." Let's hope dual air bags are standard equipment.

John McL.
Keene, N.H.

DON'T BLAME MARKET FORCES FOR BREAKING UP THE FAMILY

It is not often that one sees an article in BUSINESS WEEK containing as many misinterpretations as "Welfare reform won't patch up poor families" (Economics, Jan. 23). To argue that free markets are a major cause of the breakdown of the family, one must have a misunderstanding of economics and a serious ideological bias. To dismiss the hypothesis of Charles Murray that U.S. welfare policy has tended to encourage

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Readers Report

CORRECTIONS & CLARIFICATIONS

On page 114 in the Mutual Fund Scoreboard (Feb. 6), the head-and-shoulders outline on under "Management Changes" should indicate that a new fund manager has been in place since Dec. 31, 1993, not 1994.

Passage to India, compliments of George" (Finance, Jan. 23) incorrectly described George Soros' investment in Phoenix Information Systems. The Soros group bought \$12 million worth of stock warrants priced at \$3, \$10 million convertible note, and \$1.22 million worth of common shares. The average share purchase price was 72¢, and Soros will eventually own 32.1% of Phoenix.

"The Gene McCarthy of the war on abortion?" (News: Analysis & Commentary, Jan. 10), when Pennsylvania Governor Robert P. Casey remarked, "That's who we are, a religious people whose institutions presuppose supreme being," he said he was quoting Supreme Court Justice William O. Douglas.

The hope beneath the rubble in Japan" (News: Analysis & Commentary, Jan. 30) said Iron Corp. had to stop exporting because of the Kobe earthquake. Its exports were curtailed for one day and have since resumed.

pendency and illegitimacy ignores important and growing evidence to the contrary. To argue that more government policies and intervention will help a problem ignores 30 years of history.

Dan Coggin
Richmond, Va.

Thanks for the Economics Commentary and the article ("What to expect if welfare ends," Economic Trends, Jan. 1), challenging the assumption that welfare recipients are like the middle class, that welfare makes them dependent. Cutting aid alone won't help the marginalized person with manual-labor skills. Republicans are right: more people should work. Democrats are right: development and compassion are needed to assist those left behind.

Roger D. Harms
Wichita

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BOOK BRIEFS

WHY WE GET SICK

The New Science of Darwinian Medicine
By Randolph M. Nesse, M.D., and
George C. Williams, PhD
Times • 291pp • \$24

MISGUIDED DOCS

So many camps have co-opted the term "survival of the fittest" that Charles Darwin's theory of biological evolution has been distorted and obscured. One result is that many people erroneously believe that evolution refers to some force pushing us continually to improve, until we reach a healthy, perfected state. Another, as Randolph M. Nesse and George C. Williams spell out in *Why We Get Sick*, is that modern medicine has not adequately considered the biological origins

of many maladies and consequently may be missing out on better strategies for treating them.

In enjoyable, if sometimes too breezy, form, the authors set the record straight: Evolution relies on random mutations that happen to confer superior reproductive fitness on individuals and so are incorporated into a species over many generations. But we're not likely to evolve dramatically longer lives, because the traits that help us grow and reproduce can be deleterious, too. For example, cell division, so necessary for growth, can backfire and become cancer. But cancer typically does not hit till we're past reproductive age, so mutations that help people avoid it aren't systematically passed on.

These realities can inform smarter approaches to some health problems.

Doctors have long sought a treatment for morning sickness, for example. But some research suggests that morning sickness and food revulsion in pregnant women have evolved because they help toxins away from the fetus. The authors believe doctors should try to learn what factors are dangerous before suppressing women's natural responses. Similarly, they suggest that fevers aren't just symptoms of infection but evolved disease-fighting mechanism—so efforts to lower them may be misguided.

At times, the authors go so far as to suggest that so many evolutionary threads at work that it's hard to sort through the tangle. But *Why We Get Sick* offers both a provocative challenge to medicine and a thoughtful discussion of how evolutionary theory applies to people.

BY JOAN O'C. HAMILTON

BEYOND THE PROMISED LAND

Jews and Arabs on a Hard Road to a New Israel
By Glenn Frankel
Simon & Schuster • 416pp • \$24

DATED CLIPPINGS

In *Beyond the Promised Land*, Glenn Frankel, ex-Jerusalem bureau chief for *The Washington Post*, provides us with a great deal of reportage, some of it interesting. But somehow Frankel, who won a Pulitzer for his Mideast coverage, fails to forge the details into the larger structure needed to deliver a clear portrait of the "new Israel" promised by the subtitle. The book reads like



BEYOND
THE PROMISED
LAND

Glenn Frankel
OF THE WASHINGTON POST

a lot of newspaper and wire dispatches spliced together, and that grows tiresome.

Frankel's big theme is that the harrowing experiences of the uprising in the Occupied Territories and the Iraqi Scud attacks during the gulf war have made Israelis realize that they won't have a bright future unless they make peace with Arab neighbors. At the same time, he says, the Palestinians have undergone a similar change in attitude. So a new Israel is emerging that will be able to focus more on business and trade than on fighting for survival.

Frankel is probably right. But he

gives us mostly the old Israel: endless details about Palestinian-Israeli disputes, Israeli political intrigue, and U.S.-Israeli relations. Anyone who has read a decent newspaper over the past 10 years will find lots of this familiar.

There is surprisingly little on the new Israel of entrepreneurs and technology companies. Frankel has some good material on younger Israeli political leaders, such as Haim Ramon, who has been leading a rebellion in the Labor Party, and Likud counterparts such as Ehud Olmert, who ousted Teddy Kollek, the legendary mayor of Jerusalem.

Just now, however, Frankel's cautious optimism seems decidedly off-key. It may be that he wrote the book too soon. The peace process is in the midst of a setback, and the old stories—terrorism and other violence—dominate the news. Frankel himself has worried in the *Post* that the kind of chaos that engulfs Lebanon might take over Israeli life.

BY STANLEY REED

VISIONS OF THE FUTURE

The Distant Past, Yesterday, Today, Tomorrow
By Robert Heilbroner
Oxford/NYPL • 128pp • \$19.95

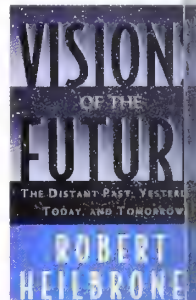
PEERING AHEAD

One vestige of the end of the cold war is a loss of familiar context. Combatants can no longer be identified as pro- or anti-communist, and competitors are as likely to be emerging nations as venerable industrial countries. How to explain this new world?

By giving it perspective. That's economist Robert Heilbroner's aim in his thin volume. Author of the classic *Worldly Philosophers*, Heilbroner draws on work from anthropology to economics to build a construct within which to view the past, understand the present, and speculate about the future.

He argues that in the "distant past"—from the time of hunters and gatherers until the Industrial Revolution—our ancestors viewed life as static; they had no expectations of change or material gain. Wealth, such as it was, went to the rulers, and poverty was seen as the natural order. "Yesterday"—the period from the Industrial Revolution until about 1950—marked a sea change as technology spurred phenomenal growth. Capitalism, with its promise of material gain, became the dominant social order. At the same time, political will became a new, revolutionary force, manifesting itself in various ways, from democracy in America to communism in Russia.

"Today," technology still fuels growth but expectations have soured. Heilbroner attributes this to a recognition of technology's dark side—from Hiroshima to Chernobyl—and the ongoing exclusion of many from capitalism's rewards. But the current anxiety, he says, could give way to an optimistic "tomorrow"—as far away as a century—if



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Books

man endeavor focuses less on accumulation and people stop viewing progress as a way to achieve heaven on earth.

Any such summary of past and future suffers, inevitably, from oversimplification, and Heilbroner is at his weakest suggesting what the future might be like. Still, for those of us groping for ways to evaluate what's happening in our brave new world, he makes a worthwhile contribution.

BY KAREN PENN

THE COLLECTED STORIES OF LOUIS AUCHINCLOSS

By Louis Auchincloss
Houghton Mifflin • 465pp • \$24.95

WASP WORLD

If you care to know how Lester Gordon acquired control of Atlantic Enterprises with Atlantic's money, resulting in the loss of his own companies, his reputation, and his wife, you must consult the Wall Street law firm of Arnold & Degener. And the only way to do that is through the fiction of New York attorney Louis Auchincloss, whose short story *The Money Judge* describes Gordon's fall. This septuagenarian writer's stock-in-trade for nearly 50 years has been a rich inventory of imaginary law firms and businessmen and the WASP Establishment of old New York. His credentials for both can't be faulted: years at Sullivan & Cromwell, membership in a patrician New York family. He also writes like an angel.

In the *Age of Newt and O.J.*, Auchincloss seems old-fashioned. Introducing these 19 stories, he acknowledges that his method of telling a tale that can range over years owes more to Edith Wharton and Henry James than to current fashion. Yet his subject matter demands his use of the slow wind. The rise and fall of law firms or family businesses is brought slowly to the light.

Auchincloss is concerned with the constraints governing conduct within an organization—and the comeuppance that awaits those who transgress. Anyone in business will immediately recognize the principals of such tales as *The Colonel's Foundation* and *The Mavericks* as people they've met before.

BY JOHN E. PLUENNE

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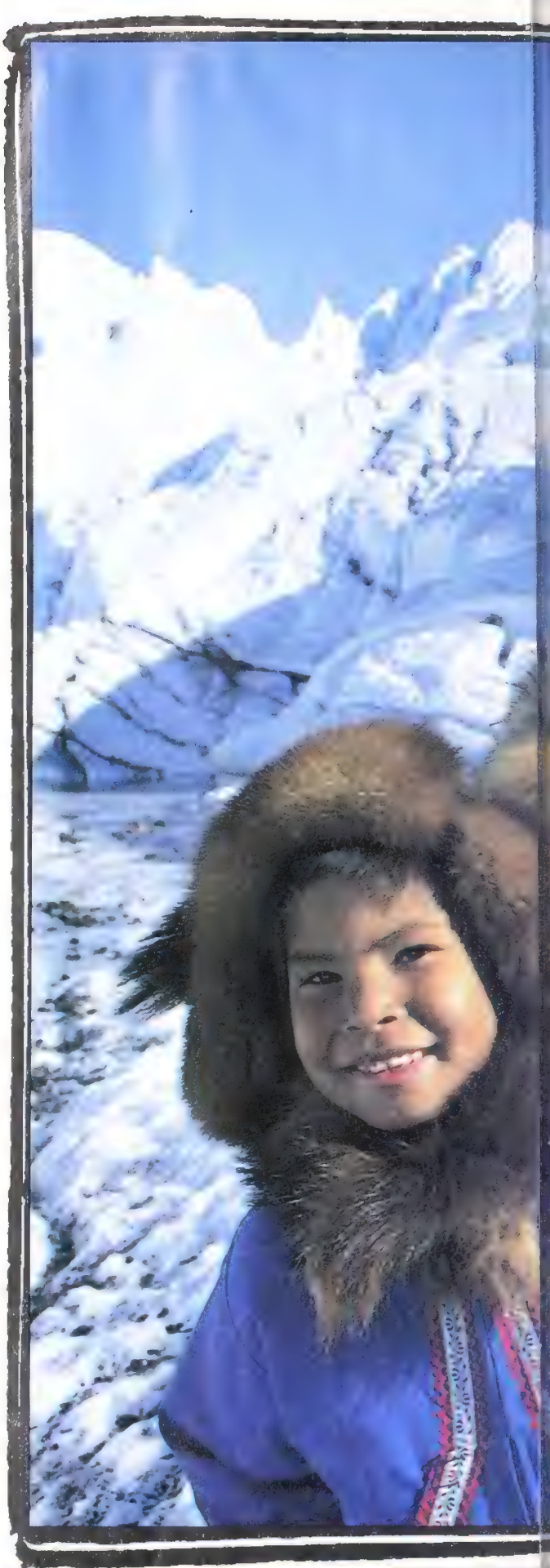
When that happens, they'll need more than just their vision to keep their companies strong. They'll need to manage a seemingly endless flow of information.

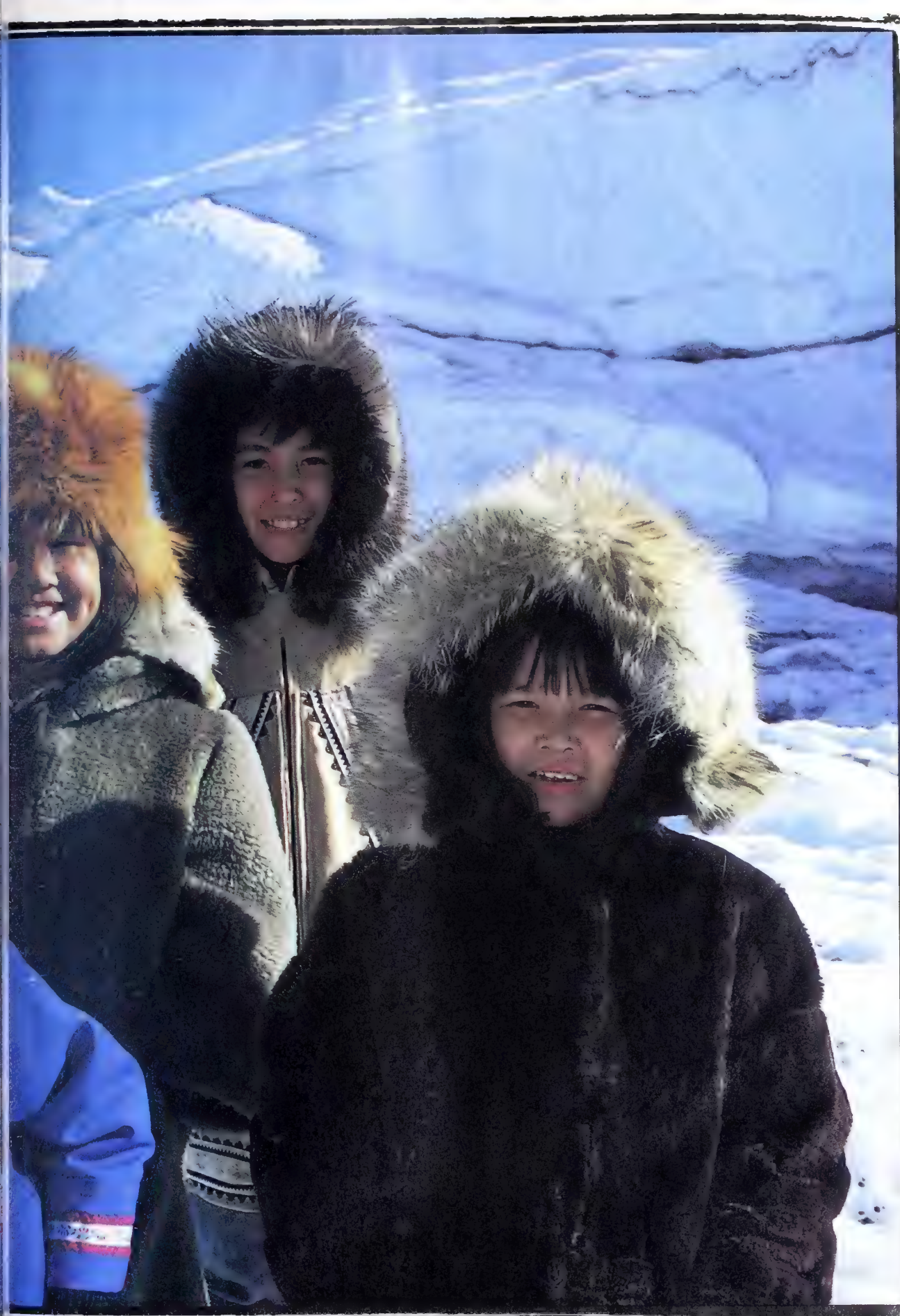
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The right information technology, however, will not.





BY STEPHEN H. WILDSTROM

THIS MAC REALLY DOES WINDOWS

It looks like the third time is the charm for Apple Computer Inc.

Last year, the company offered hardware and software that make it possible for the Macintosh personal computer to run software written for Microsoft Corp.'s Windows operating system. Both the Quadra 610 dos Compatible and Insignia Systems Inc.'s SoftWindows for the Power Mac were interesting, but suffered from a raft of problems.

With the introduction of the Power Macintosh 6100/66 dos Compatible, Apple has finally done it right. Press two keys on your Macintosh and you can switch from your favorite Mac program into a zippy Windows environment. Apple also offers an add-in Compatibility Card for existing Power Macs (table).

The compatible can spare you the need for two computers if your kids want a Mac like the ones they use in school, but you need to run PC-based office software. Mac fanatics who work in PC shops may be able to have it both ways.

TWO BRAINS. Apple works its magic—the product was code-named Houdini during the development stage—by building two computers into one box. Each has its own processor (a 486DX2 for the PC), memory, and display circuitry. The two share disk and CD-ROM drives; audio, keyboard, and mouse; and

printer, modem, and network connections. And there appears to be no speed penalty except when the two programs attempt to use the same disk drive or other function at the same time.

My informal testing indicates that Apple has achieved a high degree of compatibility on the Windows side. Multimedia programs that have given me trouble on some pure Windows ma-



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DATA APPLE COMPUTER INC., RELY CORP

chines, such as WordPerfect Corp.'s Wallobee Jack games, ran flawlessly.

Earlier attempts at dual-mode Macs lacked support for DOS or Windows networking. But I got the new DOS Compatible running on our Novell NetWare network in a snap: Like all Macs, networking is built in, and the Windows side is easy, too.

Indeed, I could find only two major areas of incompatibility, and Apple alerts users to both. The Macintosh mouse is equipped with only one button and you have to use the keyboard to simulate the right mouse button that's used in Windows. And Macs and PCs use entirely different hardware to connect with modems. Results are variable: Stac Electronics Inc.'s Reach-Out remote-control software worked fine, while America Online dialed the telephone but couldn't connect.

Previous efforts at compatibles flopped because they were sluggish, and couldn't run multimedia programs or connect to networks in Windows and DOS. The new system hits equally well from either side of the plate.

"RIGHT THING." Apple, which has no desire to encourage its customers to move toward Windows, is focusing sales on PC owners and first-time buyers. "If we were only selling to the installed base, we'd wonder if this was the right thing to do," says Dave Daetz, Apple's product line manager.

Indeed, Apple is leaving its brand name off compatibility retrofits for the mass of Mac owners. Instead, it has licensed the technology to Rely Corp. (800 801-6898), which offers a range of boards for Macs powered by Motorola Inc.'s 68040 chip.

To attract new buyers to Macs, Apple is pricing the package aggressively. When the machine hits retail outlets in quantity in February, it will probably be available with a keyboard, monitor, and CD-ROM for under \$3,000, perhaps \$500 more than a similar PowerMac without PC compatibility.

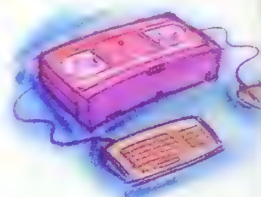
A switch-hitting Apple isn't for everyone. But it resolves a lot of dilemmas for both homes and offices where Macs have been lovable but impractical.

BULLETIN BOARD

SOFTWARE

VIDEO EDITOR FADES IN

It may not make you a Spielberg or a Fellini, but professional-quality video editing is now within reach of anyone with a Macintosh. For \$259, Video Shop 3.0 from Avid Technology Inc. (800 949-2843) turns you



Mac into an editing machine with a simple visual interface that handles transitions, special effects, audio, and titles on a frame-by-frame basis. Any color Mac can edit images in memory. Working from videotape requires a VCR and either an A/V model Mac or a video digitizer, such as the Radius Spigot, starting at about \$500.

TELECOM

AREA CODE MELTDOWN

New area codes are giving lots of business phone systems fits. Starting on Jan. 1, metro Chicago, western Washington State, and southern Alabama got the first area codes that don't have a 1 or a 0 in the middle, and many business callers were unable to read the new numbers. That's because their PBXs didn't recognize the new codes as valid. With several more such codes scheduled to take effect this year, Bill Todd, external affairs manager for BellSouth in Birmingham, cautions businesses to make sure that their PBX software is up to date.

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BY RUDI DORNBUSCH

WHY IS THE MIDDLE CLASS REALLY BOGGING DOWN?



HARD WORK:

The reasons are complex, but class warfare isn't one of them. So Clintonites should can the rhetoric and push to keep growth robust

The battle for 1996 is on: President Clinton is fighting for survival by invoking divisive class prejudice, while the Republicans are no better in their promise to create prosperity out of thin air. The economy has been doing well, there has been growth, and there is full employment. But it is obvious from the political maneuvering that more is expected and promised than the economy can deliver. That is a dangerous route: Even a free-market economy cannot deliver equality and prosperity for all.

Today, the U.S. economy is operating at peak performance. Over the past decade, growth has been strong, averaging 3% a year including the last recession. Unemployment is as low as it can get before inflation becomes the dominant issue. So why does the average American feel left out, even betrayed?

During the 1950-73 period, median family income doubled. That has been the American model—every generation gets ahead of the previous one, with the postwar decades representing a giant advance from the Depression years. But since the early 1970s, the economy has failed to deliver broad-based income gains. Even though the economy has grown steadily, the average American family is basically where it was 20 years ago. Poverty rates have increased, and the economic foundation of the middle class is being eroded.

COSTLY MINIMUM. There is no single explanation for the middle class bogging down. A list of contributing factors would include fewer unions and monopolies on which they can feast, more competition within the country and across borders, immigration, deregulation, and labor-saving technology. More broadly, the shift to an immensely competitive environment, where the norm is cost-cutting and paying no more than the bare minimum, has been ruinous to the middle class.

Over the past decade, much of the success in cost-cutting has not come from raising output per worker hour. It has come from reducing labor costs by shifting work outside the company or across borders. It's no surprise if companies have photocopies made at the minimum-wage-paying shop across the street rather than in-house at middle-class wages. And advances in transportation, communication, and information technology have created one vast world labor market, making a leveling inevitable.

What to do about all this? One answer is to

roll back progress, making competition its forms the enemy. That is impossible. Europe is finding that its proclivity for a protectionist welfare state that shelters workers and wages from market pressures has become a costly aberration—and undesirable. Without competition and progress, there is no assurance that real income will grow again. Even if income grows, what to do about rising inequality? The common-sense answer must be that more growth provides a bigger pie, and this must remain the priority. There are three ways to create more growth, none of them new and all of them hard work: better education for the middle class, freer trade to empower high-wage industries, and a far higher rate of investment.

MALIGNANT NEGLECT. The safest way to get investment up is to cut the deficit, and there is no better time to do so than at full employment. Much of the political debate has fought around the status quo: shifting tax burdens and expenditure benefits around like furniture while neglecting potential private budget-savers that have so far been protected by Congress. Robert J. Shapiro of the Progressive Policy Institute has identified spending and tax reforms that would result in total five-year savings of \$225 billion. That is a good downpayment for tax cuts and deficit reduction.

There is also an important political message in a key Clinton Administration mistake that some have lauded as a great political ploy. With characteristic skill, White House spokesmen repeatedly acclaim “working-class families who play by the rules.” The argument runs like this: If the economy is going ahead and most people are not, someone must be making off with the money. Today, corporations are routinely pictured as greedy, unfair, and exploitative, and the middle class portrayed as getting the shaft. The notion that corporations should make profits is no longer acknowledged.

The Administration's rhetoric only incites class warfare. In the context of inequality, too little is said of individual responsibility, education and skills and too much of how the system is flawed. It undermines the basic American expectation that anyone who tries hard enough can get ahead. To declare the basic premise null and void creates a social pessimism that opens the door to questioning a free, competitive society.

Rudi Dornbusch is professor of economics at Massachusetts Institute of Technology

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"The reasons we Daytime Running



You're driving in broad daylight. Suddenly, a car's lights catch your eyes. They could be new daytime running lamps (DRLs). These special low-intensity headlights help alert other drivers with light, like your car horn can alert them with sound, according to Minotas, a member of General Motors' safety team. They're simple, practical, and easy to

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"Lamps are obvious."



General Motors.

because they come on automatically. And research shows they reduce collisions, and that help save lives. GM is introducing daytime running lamps in 1995, and they'll be shining all its vehicles by 1997. Right now, no other domestic auto company offers them. Jay says hopes that will change: "The sooner every car and truck has DRLs, the safer we'll all be."

BY GENE KORETZ

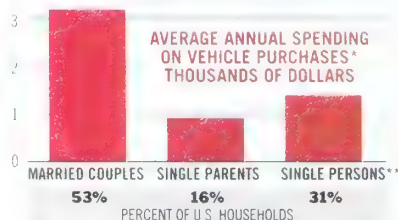
A YELLOW LIGHT FOR DETROIT

Demographic trends are worrisome

It is eight years since U.S. car and light truck sales hit a record 16.1 million clip. Yet four years into the current expansion, vehicle sales still lag behind their prior peak. And a big reason, says economist Paul D. Ballew of the Federal Reserve Bank of Chicago, is the startling growth of nontraditional households and their adverse impact on purchases of big-ticket items like cars.

From 1970 to 1992, note Ballew and economist Robert H. Schnorbus of the Chicago Fed, as the U.S. added more

HOW HOUSEHOLD TYPES AFFECT AUTO OUTLAYS



*NEW AND OLD VEHICLES IN 1992

**INCLUDES SINGLE PERSONS LIVING TOGETHER

DATA: FEDERAL RESERVE BANK OF CHICAGO

than 32 million households, the share made up of married couples, with or without children, shrank from 77% to 53%. At the same time, the shares of one-parent and single-person households jumped to 16% and 31%, respectively.

These changes spell increasing income inequality. Over the 1970s and '80s, real median income of U.S. married couples rose 13%, as women flooded into the labor force. Single-parent and single-person households, by contrast, saw little or no income growth, and their median incomes are now less than half of married couples'. (Almost a third of single-parent families and a fifth of single persons live below the poverty line).

The growth of nontraditional households has already begun to exert increasing downward pressure on vehicle sales and other major consumer purchases. In 1992, for example, average outlays for car purchases (new or used) by single parents was only 29% of spending by married couples, while such outlays by single persons were 56% below married-couple levels (chart).

With a third of all American children

now born to single women, the economists think the impact of such trends on consumption patterns—and on the entire economy—will intensify in the decades ahead. And though the effect initially may spur demand for economy and used cars, they warn that eventually it could result in a period of sales stagnation.

WHEN THE BOSS HAS A BIG STAKE

Simply put, shareholders do better

Do shareholders tend to profit when top executives have a sizable stake in the fortunes of their companies?

To find out, Wyatt Co. recently analyzed the stock market performance of 105 large U.S. companies over a five-year period in relation to company shares owned by their chief executive officers. Ownership was defined as the ratio of the dollar value of a CEO's holdings (excluding stock options) to his or her base salary.

Wyatt found that the top half of the companies in terms of chief executive ownership posted average annual returns of 11.4% over the five years, compared with 7.3% for those in the bottom half. The results, which were similar when industry groups were analyzed separately, suggest that it can pay to invest in companies whose bosses have a lot riding on their performances.

HOORAY FOR RISING RATES?

The gain may exceed the pain

Although some economists argue that rising interest rates squeeze consumers more than they help them, Edward F. McKelvey of Goldman, Sachs & Co. disagrees. He notes that industry and Federal Reserve sources estimate that only a third of all mortgages and revolving credit balances, currently about \$3.1 trillion and \$328 billion, respectively, are adjustable-rate. That's some \$1.15 trillion in liabilities.

On the other hand, McKelvey calculates that households own about 1.7 times that amount, or \$1.95 trillion, in assets whose returns can change over a year's time. This includes about \$469 billion in time deposits and Treasury securities maturing within a year, \$330 billion in money market funds, and \$1.15 trillion in savings deposits that can be

moved if their rates rise too sluggishly.

What's more, since rate hikes on most adjustable-rate mortgages, which account for the bulk of interest-sensitive household liabilities, are capped at 0.5 basis points a year, McKelvey calculates that the household sector's maximum exposure to rising interest rates on current liabilities is about \$22 billion a year. By contrast, the interest individuals received over the latest 12 months, minus so-called imputed interest, came to an annualized \$33 billion—indicating, says McKelvey, that "rising rates are putting more income into the pockets of families than they are taking out in the form of larger debt-service payments."

BORDERS ARE FOR CROSSING

Dealmakers take a worldwide view

Sparked by a brisk global economy, merger mania surged to new heights last year. According to a tally by KPMG Peat Marwick, the number of cross-border acquisitions, joint ventures, and minority investments rose 20% to 5,400 in 1994. Total value of such deals, including 40 in the \$1 billion-plus range, soared 46% to \$239 billion.

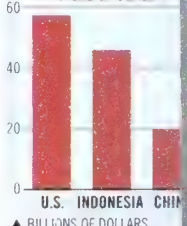
The leading investment targets in terms of deal values were the U.S., Indonesia, and China (chart). (Indonesia snared a \$40 billion investment by Exxon Corp.) China was second in the number of such deals, attracting 490, compared with 668 for the U.S.

Among investors, the biggest spenders were the U.S., which shelled \$87 billion, \$30 billion more than it attracted, followed by Britain (\$38.2 billion) and Switzerland (\$16.3 billion). While U.S. companies were particularly busy in Britain, Spain, and China, the Mexican transactions fell almost in half to \$1.5 billion, while Mexican deals the U.S. nearly tripled, to \$1.4 billion.

As for industries, the top four cross-border deals were petroleum and mining (\$59.6 billion), information, communications, and entertainment (\$23 billion), chemicals (\$23 billion), and food (\$14.1 billion).

1994'S GLOBAL MERGER MANIA

THE BIG THREE CROSS-BORDER TARGETS (BASED ON DEAL VALUE)



▲ BILLIONS OF DOLLARS

*ACQUISITIONS, JOINT VENTURES AND MINORITY INVESTMENT

DATA: KPMG PEAT MARWICK

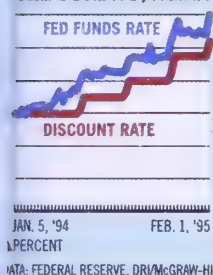
JAMES C. COOPER & KATHLEEN MADIGAN

HOW IS THE FED READY TO STOP TIGHTENING THE VISE?

U.S. ECONOMY No good deed goes unpunished. Neither does a good economy. The fourth quarter's burst of growth capped off the economy's best performance in 10 years, even as inflation remained quiescent. And according to the early data for January, consumers and businesses carried some of that momentum into the new year.

The result of such uplifting news: The Federal Reserve tightened the monetary screws for the seventh time in a year. On Feb. 1, policymakers at the central bank voted to raise the federal funds rate by half a percentage point, to 6%. The fed funds rate, which banks charge each other for overnight loans, has doubled in the past year. The Fed also bumped up the discount rate it charges banks for loans by a half point, to 5¼% (chart).

THE FED TURNS THE SCREWS, AGAIN



In its statement regarding the hikes, the Fed said: "Despite tentative signs of moderation in growth, economic activity has continued to advance at a substantial pace, while resource utilization has risen further." That's the first time a policy statement has acknowledged even a hint of a slower economy. But the financial markets reacted negatively because the statement did not give a clearer signal that the Fed was finished tightening.

4.5% ANNUAL RATE of growth in the fourth quarter's real gross domestic product wasn't unexpected, but the Fed was undoubtedly displeased that demand remained so resilient despite its past rate hikes. Final demand grew 3.7% last quarter, slower than in the third quarter, but excluding the ups and downs in defense outlays, demand increased a sturdy 5.1%, faster than in the previous quarter. In fact, the hot items last quarter were durable goods—the very items sensitive to interest rates. The real head-turner in the GDP report, though, was another huge rise in inventories. Total inventories grew by \$8 billion last quarter, after mega-increases of \$59.2 billion

in the second period and \$57.1 billion in the third (chart). That's the largest three-quarter accumulation in a decade. But while the buildups in the two prior quarters were intentional, the yearend increase may have been more than businesses wanted. That's because, according to the Commerce Dept.'s estimate, the biggest gain came during December, when consumer spending began to flag.

The inventory pileup has three implications for 1995. First, most of the extra inventory ended up in the warehouses of wholesalers and retailers. So these businesses will have little need to re-order goods, leading to smaller gains in factory output and jobs in coming months.

Also, look for a lull in the import surge because some of those warehoused goods were made overseas. The import slowdown will help reverse the widening of our trade deficit. In the fourth quarter, imports grew 16%, outpacing the 14.2% advance in exports and widening the net-export deficit by \$7.1 billion. The \$124.1 billion gap was the largest in seven years.

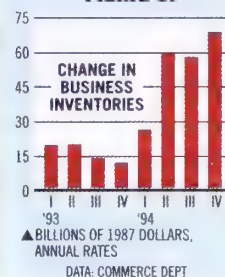
And last, unwanted inventories will help the inflation outlook. With retailers overstocked, stores will have to cut prices to clear out excess merchandise. That means inflation at the consumer level should remain low.

BUT FOR HOW LONG? The fourth-quarter GDP numbers indicate that U.S. output of goods and services is now greater than the output possible when all labor and capital resources are fully utilized, according to the Fed's numbers. With demand outpacing the ability to satisfy it, price pressures typically emerge. So inflation hawks are worried that the best inflation news is now behind us. Inflation, as measured by the GDP fixed-weight price index, shows some acceleration, rising 2.9% in the year ended last quarter. That's up from a 2.5% rate in 1994's first quarter.

Price pressures were also on the minds of the nation's purchasing agents in January. The National Association of Purchasing Management said its index of prices paid by manufacturers held near a 15-year high, and that business activity began 1995 with "a good head of steam." The NAPM's index rose to 57.9% from 57.5% in December.

The reports of industrial price hikes as well as the imbalance between real GDP and its potential are the chief reasons why the Fed acted to restrain the economy even

INVENTORIES ARE PILING UP



more. So far, though, only a few signs of slowing are emerging. Last quarter, home construction fell at a 2.6% annual rate. The dip would have been larger if not for unusually mild weather. Consumer spending slowed over the course of the three-month period, but buying surged by 4.6% for the quarter.

Consumers saw their real aftertax income jump by 0.7% in December, but they lifted their inflation-adjusted spending by only 0.2% after a modest 0.3% increase in November. They may have started to realize that higher adjustable-rate mortgage payments and large credit-card bills lie ahead.

Consumers gave a mixed appraisal of the economy in January. According to the Conference Board, consumer confidence edged down to 102.1 from December's 103.4. While a reading above 100 indicates an upbeat view, consumers' plans to buy interest-sensitive goods declined. Intentions to purchase a new car dropped sharply, plans to buy appliances fell for the second month in a row, and home-buying plans have been drifting lower since August.

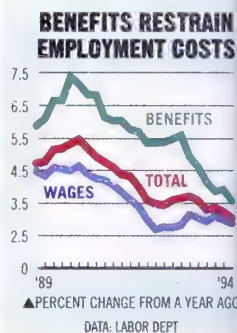
THE FED had to be heartened by the benign pattern of labor costs in 1994. Wages and benefits for civilian workers rose 0.7% last quarter and just 3% for the year—down from 3.5% in 1993, and the smallest gain since the Labor Dept. began tracking employment costs in 1981.

The slowdown in compensation was evident in al-

most all occupations and industries. Wage growth continued to drop, falling to 2.8% in 1994 from 3.1% in 1993. But benefits staged a more dramatic slowdown (chart), growing only 3.4% in 1994—way below the 4.6% gain in 1993 and about half of the 6.7% in 1990. Lak said the small rise reflected slower growth in health and workers' compensation insurance costs.

However, last year may have been the bottom for labor-cost growth. Hourly wage gains started to edge higher in the second half of 1994. And with labor markets growing tighter, businesses may have to loosen their purse strings and lift pay to attract qualified workers. Even so, the forces of intense competition and increased productivity will keep the growth in unit-labor costs mild even for 1995.

The problem for those hoping to find a job or expand business is that even a mild acceleration in labor costs may be too much for the Fed. That means the central bank will not stop hiking rates until the economy shows broad signs of slowing down. Only then can the inflation-wary Fed be certain that price pressures are in danger of bursting out of control.



ASIA

CHAMPAGNE AND PROZAC FOR HONG KONG'S NEW YEAR

Hong Kong's stock market will have a lot to digest when it reopens on Feb. 3, after the observance of the Chinese Lunar New Year. Consider the worry list: rising interest rates, falling property prices, souring Sino-American trade relations, prospects for slower growth in China, and uncertainty surrounding Deng Xiaoping's failing health. It's little wonder that the Hang Seng stock index, already in a yearlong decline, has plunged 23% since Nov. 16.

However, the bear market is now well advanced, based on past experience, and it may be close to its nadir, say many analysts. Property stocks rallied after the government

land auction on Jan. 25, suggesting some life in the real estate sector (page 60). Some 70% of Hong Kong's businesses derive a portion of their earnings from real estate.

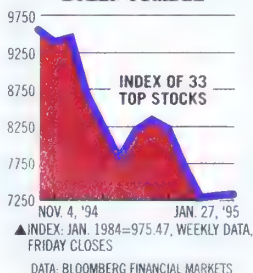
Property values have been hit especially hard by hikes in U.S. interest rates, which have pushed up rates in the territory, since the Hong Kong dollar is closely tied to the U.S. dollar. But after the Federal Reserve's hike on Feb. 1, speculation is growing that Fed tightening is about finished for this cycle.

Many fear that a China-U.S. trade war would dent Hong Kong's huge reexport business. Reexports—goods made elsewhere but

shipped through Hong Kong—account for 80% of the territory's exports. However, reexports from China have been slowing for three years, as growth on the mainland has cooled off from 13% in 1993 to 11% in 1994 to a projected 9% this year, and as China's shipping capacity has increased.

Most observers expect Hong Kong's economy to grow 5.5% this year. High rates and a plunging stock market have depressed consumer incomes and spending. But persistent, if slower, growth in China and better growth globally in 1995 will continue to power exports. In the short term, share prices will remain vulnerable until current worries ease. But further out, Hong Kong is well positioned as the financial center of the world's fastest-growing region.

THE HANG SENG'S STEEP TUMBLE



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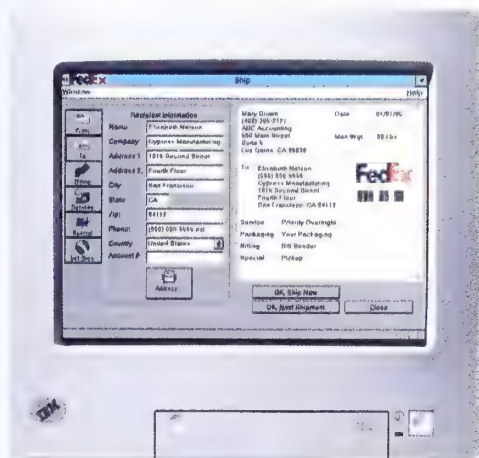


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THE MEXICAN CRISIS

ANATOMY OF A RESCUE MISSION

How Clinton cobbled together an aid package as Congress waffled

The call came to the White House at 8 p.m. on Jan. 30. It was House Minority Leader Richard A. Gephardt (D-Mo.), and the news was bad: President Clinton's controversial \$40 billion loan-guarantee plan to prop up the Mexican peso was dead on Capitol Hill. With stock markets from Brazil to Thailand shuddering at the prospect of a Mexican government default, top Administration officials labored through the night to craft an alternative plan.

Bleary-eyed Treasury Dept. officials quickly cobbled together an international peso posse. After getting the legal O.K. to draw \$20 billion from a discretionary Treasury fund normally used to support the dollar, Treasury Secretary Robert E. Rubin and his top international strategist, Lawrence H. Summers, phoned French and German Finance Ministers in a desperate race to line up billions more in international support. The final piece of the package fell into place at 5 a.m. on Jan. 31, when the International Monetary Fund reluctantly agreed to kick in \$10 billion on top of \$7.8 billion it had pledged earlier—a record commitment from the fund.

By dawn's early light, Treasury had Plan B in place. The bottom line: a \$49.8 billion package—remarkably similar to the original bailout—that averted a meltdown in the world's financial markets. "The risks of inaction are greater than the risks of decisive action," Clinton declared later that morning to a meeting of state governors. "This is the right thing to do."



RELIEF PITCH: Clinton managed to extract GOP leaders' support for his plan.

The revised rescue comes with plenty of strings attached. Mexico will have to cut government spending, slow the growth of private credit and its money supply, and sell off more state-owned industries. And Mexico will have to fork out hefty fees for the right to tap \$20 billion in U.S. loans or loan guarantees, which will make it easier for the government to borrow in commercial markets. But since the plan will bypass Congress, there are no politically touchy demands to improve labor standards or border controls on migration, two conditions sought by U.S. lawmakers. For now, the bailout appears to be

working. Jittery foreign investors, who saw their Mexican holdings eroded by a 45% collapse in the peso since December, were looking on the bright side. By Feb. 1, stock prices on the Mexican *bolsa* were up 5.2%, and the peso rose 18% to 5.4 to the dollar. "The President's decision helped stabilize other markets as well as Mexico's," says Arthur J. Massolo, head of the Latin America division at First Chicago Corp.

On Capitol Hill, the plan was a godsend. A month earlier, Congress would have squawked at Clinton's unorthodox use of the Treasury's stabilization fund. Indeed, Federal Reserve Chairman Alan

Greenspan told a Senate committee on Jan. 26 that the Fed and Treasury lack authority "as we see it to take that sort of action." But now most lawmakers are pleased they won't have to vote on a highly unpopular bailout. "There was a sigh of relief here," says Representative Sander Levin (D-Mich.). "Most [members] will welcome it without saying so."

Throughout Corporate America, Mexico-minded executives could only hope that the worst was over. Ford Motor Co.'s plans to double vehicle shipments to Mexico to 50,000 this year is now "a pipe dream," says CEO Alexander J. Trotman, though Ford says it's sticking with plans to shift some operations south of the border. Adds Nicholas F. Fiore, senior vice-president of Carpenter Technology Corp., a Reading (Pa.) steelmaker: "We expected short-term setbacks and windfalls, but we wouldn't have gone in if we weren't in for the long haul."

The massive international bailout plan rapidly organized by distressed U.S. officials signals a seismic shift in the global financial order. Just as the American public and Congress are growing weary of the U.S. military shouldering sole responsibility for policing the globe, America's days of being the emergency banker for every financial crisis may be over as well. Deal broker? Yes, Washington will continue to lead. But, says a senior Administration official, "the U.S. cannot be the world lender of last resort" (page 38).

TOURNIQUET. In an era of quicksilver capitalism, global-market panics will likely become more commonplace. But playing commander-in-chief of the international bucket brigade poses political risks for Clinton. His authority is already under attack at home by a new breed of populist lawmakers wary of foreign entanglements (page 35).

At this point, concerns about Clinton's political future pale in comparison to worries about Mexico's economic outlook. Whether the bailout is a long-term solution or a tourniquet ultimately depends on Mexico's willingness to swallow harsh economic medicine (page 36). Meeting the stiff economic conditions "will just put Mexico into a big recession, and it is not clear how the country will come out of it," says Rudi Dornbusch, an economist at the Massachusetts Institute of Technology. David Hale, chief economist of Kemper Financial Services, fears that even with new help, the peso's downward spiral will triple the size of nonperforming loans at Mexico's undercapitalized banks to about

EXECUTIVE ORDER 44 The risks of inaction are greater than the risks of decisive action. This is the right thing to do. — BILL CLINTON



Clinton's New Deal For Mexico

Details of the \$49.8 billion aid package assembled by the U.S.

TREASURY By executive order, Clinton will provide \$20 billion in aid with terms of as much as 10 years by tapping the Treasury's Exchange Stabilization Fund—normally used to bolster the dollar.

FEDERAL RESERVE The Fed will make available \$4.5 billion to Mexico in short-term loans until the promised longer-term Treasury financing is issued to Mexico.

INTERNATIONAL NATIONS Major industrial countries will kick in \$10 billion in aid in the form of credit through the Bank for International Settlements. In addition, Canada pledged \$1 billion and Latin American nations \$1 billion.

The International Monetary Fund will provide \$10 billion in five-year loans on top of the \$7.8 billion in credit it already has promised Mexico.

IMF The U.S. and IMF will insist that Mexico adhere to strict targets for money supply, domestic credit, fiscal spending, and foreign borrowing. U.S. loan guarantees will be backed by oil-export revenues to be deposited at the Federal Reserve Bank of New York as collateral.

DATA: U.S. TREASURY DEPT., INTERNATIONAL MONETARY FUND

30% of their portfolios. "The chances for bank failures are very high," he warns.

Many traders believe that the package will enable Mexico to lessen its risky dependence on short-term dollar-denominated securities known as *tesobonos* in favor of more stable, long-term financing. But others say that Mexicans must go far beyond the reforms called for in the bailout to bolster

than Clinton let on. Commercial banks led by Citicorp and J.P. Morgan & Co. may still come through with \$3 billion in loans announced in December. Ultimately, including the private money, the final package could top \$55 billion.

The outcome is hardly what the Clintonites were expecting when they fashioned the original \$40 billion bailout package in mid-January. Congressional leaders signed on quickly, and approval

surprising and furious revolt against House Speaker Newt Gingrich (R-Ga.). "Newt went out to lead his Republicans, only to learn they weren't following," says one leadership aide. When Gingrich privately admitted he was one of chits after coercing freshmen to back a watered-down balanced-budget amendment, Clinton feared the worst.

NAILED DOWN. News that the plan was faltering spread quickly across the globe. At a world economics conference in Davos, Switzerland, a GOP lawmaker privately confessed to international financiers on Jan. 28 that the rescue plan didn't even have the support of 10 House members.

That helped trigger a Monday morning sell-off in Latin American markets. By noon, the Brazilian *bolsa* had plunged 8%, and the Mexican peso was on its way to a further 15% collapse. Even as Rubin was trumpeting the support of former Presidents and Secretaries of State at a press conference, Summers was warning senators that Mexico's currency reserves were so low that it could default within 48 hours. Efforts to nail down Plan B began the evening.

Clinton, his all-night plan in hand, summoned congressional leaders to the White House early Tuesday morning. Is there any hope for a vote turnaround, he asked. "You will have to go in the trenches and fight it out member by member," Gingrich advised. That day, Clinton unveiled the new package and demanded that the leaders publicly back him. All agreed, and the group sneaked out a side door to avoid talking to reporters.

While the Administration's fumbling of the \$40 billion bailout dismayed Washington insiders, the speed with which Clintonites assembled the fallback financing impressed many Washington Streeters. In the first real financial crisis sparked by fears of a global run on mutual funds, the new rescue plan may usher in an era of financial cooperation among governments. If so, the U.S. just took a first step toward creating an international safety net to cushion the impact of panics that are sure to proliferate in markets that now move at the speed of light.

By Dean Foust, Susan B. Garland, Douglas Harbrecht, and Richard S. Dunham in Washington, and bureau reporters

Why Clinton Bailed Out of the Bailout



GINGRICH



DOLE



GRAMM



RUBIN

TOO LITTLE CAPITAL The President didn't invest enough political capital to win over Congress. Instead, he gave only brief, tepid support. Why? Clinton may have been reluctant to distract attention from his renewed focus on middle-class issues.

FRESHMAN REVOLT Clinton and Republican leaders underestimated the resistance from first-term lawmakers—many of whom had campaigned on slashing foreign aid. That left House Speaker Gingrich out on a limb.

GOP INFIGHTING The issue became a showdown between two Republican Presidential rivals. Senator Phil Gramm (Tex.), a conservative leader, criticized the plan in part to distinguish himself from Senate Majority Leader Bob Dole (Kan.), the front-runner for the 1996 nomination.

TREASURY NEWCOMER Treasury Secretary Robert Rubin knows financial markets but lacks political savvy. Rubin wasn't helped by his top international specialist, Under Secretary Lawrence Summers, who was unwilling to provide Congress with details of the rescue plan.

their economy and rebuild investor confidence. "The best thing they could do is what Argentina has done—open everything up to foreign investment," says Lawrence D. Krohn, head of Latin American research for Union Bank of Switzerland.

Traders and analysts still have serious reservations about whether the plan is sufficient to fully shore up Mexico's wobbly finances. And they question the willingness of Mexicans to accept promised wage hikes of just 7% after a 45% devaluation. Yet they are encouraged that the new package may actually be larger

than Clinton let on. As late as Jan. 24, House Banking Committee Chairman James A. Leach (R-Iowa) had won liberal Democrats over with concessions requiring Mexico to upgrade labor standards. The chief Democratic vote-counter, Representative Barney Frank of Massachusetts, promised up to 130 Democratic votes.

But the compromise unraveled when GOP leaders ordered Leach to yank the labor concessions. Lawmakers, frustrated that Summers and Rubin didn't provide details of the plan, began equivocating. Feisty GOP freshmen mounted a

Will Plan B do the trick? Yes, analysts say, if it's met by Mexican reforms that renew investor confidence

COMMENTARY

By Paul Magnusson

IF CLINTON AND CONGRESS CAN'T AGREE ON MEXICO...

The sun surely would have broken through the wintry gray clouds passing over the White House if President Clinton signed legislation granting Mexico \$40 billion in loan guarantees. Pocketing the ceremonial pens, smiling Republicans and Democrats might have talked of further joint efforts on even tougher economic measures to come: reforming the creaky U.S. tax structure, rescuing Social Security and Medicare, balancing the budget.

But there will be no legislation and no souvenir pens. Bill Clinton's first attempt at enlisting cooperation from GOP leaders collapsed unceremoniously on Jan. 31. What aid will be provided to Mexico instead will come from existing U.S. lending programs and from international contributions. And while Mexico may benefit, the aid debacle reads ill. "The fact is, we're not going to be working very closely with the Republicans on a lot of policy this year," laments one Administration economic official. "There are just too few areas of agreement."

Philosophical differences are natural to the two-party system. But what's ominous about the Mexico loan collapse is the inability of either the White House or congressional leaders to deliver votes from within their own parties. The GOP insisted that more Democrats in Congress stand up for Clinton's deal. But when all they got was lukewarm support from House Minority Leader Richard A. Gephardt, Republicans balked. None wanted to risk seeming too cozy with foreigners or wealthy bondholders.

LEGISLATION STEPS. But this "After you, Alphonse" routine isn't going to get much legislation passed. The Mexican rescue would have been simple compared with the economic conflicts that Congress and the White House must tackle over the next two years. For example, nearly all lawmakers are committed to wel-

fare reform, but their proposals run the gamut from expensive orphanages to ending federal welfare entirely. A compromise will require precisely the sort of strong leadership missing from the Mexico plan.

Yet the President is using the same weak tactics on welfare reform and a proposed minimum-wage hike that he attempted with the Mexican deal. He prefers to nego-

laserlike on getting it done," says Senator John McCain (R-Ariz.).

Republicans also have shown reluctance to take the steering wheel. Senate Majority Leader Bob Dole (R-Kan.) quickly endorsed Clinton's Mexico aid plan but then waffled. So did House Speaker Newt Gingrich (R-Ga.). Noting on Jan. 27 that GOP support was "eroding," Dole complained that "something dramatic's got to happen."

As if a 45% peso devaluation and impending loan defaults by Mexico weren't sufficient drama.

HEAVY WORKLOAD. The same scenario is playing out in the fiscal 1996 budget debate. Republicans are back "worshiping at the altar" of a balanced-budget amendment but are nervously ducking the collection plate—refusing even to outline proposed spending cuts until they see the Administration's draft first. Meanwhile, the most important budget issues already are missing from the table. Gingrich said no changes would be made to Social Security "for four or five years," and Democrats have shown scant interest in touching the issue. Medicare is ripe for reform, says Gingrich, but the White House seems intent on using Medicare cuts to pay for health-care reform.

To be sure, the Administration did some things right on Mexico, such as persuading Federal Reserve Chairman Alan Greenspan to help sell the package. And preparing a quick fallback plan that uses the existing Exchange Stabilization Fund averted a larger crisis. Still, Clinton and the GOP leaders in Congress will have to work harder on the really difficult economic issues—and get their respective teams on board. As a warmup for the big battles to come, the Mexico bailout should provide some lessons on how not to do business.

Magnusson covers economic policy from Washington.



CAPITOL HILL ROOKIES: In no mood to compromise

tiate details of a welfare overhaul with Congress and state governors before submitting any bill. And after agonizing for weeks over the minimum wage, Clinton still had no bill to show legislators after endorsing the idea in his State of the Union message.

Such delays can choke off legislation. Clinton's hesitancy gave opponents of the Mexico plan time to object and gave fringe players such as Ross Perot and Patrick J. Buchanan openings to lambaste it as a Wall Street rescue. "There wasn't immediate follow-through, and with a problem like this, the President has to drop everything else and focus

THE MEXICAN CRISIS

MEXICO IS STILL IN A WORLD OF HURT

Zedillo faces widespread economic pain, with no easy remedy

After a month of 20-hour workdays spent sorting out Mexico's financial crisis, Finance Secretary Guillermo Ortiz looked understandably tired on Jan. 31. Tired but, for once, satisfied: Hours earlier, the Clinton Administration had unveiled a \$49.8 billion rescue package for Mexico's embattled peso. "The times ahead of us won't be easy times," Ortiz warned.

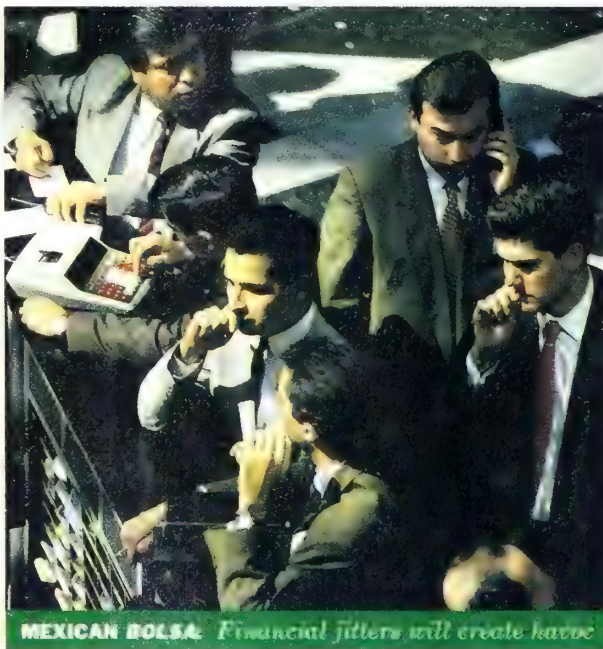
What an understatement. The devaluation of the peso and the accompanying financial jitters will dramatically slow Mexico's economy this year, as interbank interest rates as high as 50% choke off consumer spending and send overleveraged companies into bankruptcy. With emergency cuts in government spending, the economy could actually shrink by 1.5%—a far cry from the 4% growth President Ernesto Zedillo Ponce de León forecast just six weeks ago. Tens of thousands of Mexicans will lose their jobs, and inflation as high as 40% will savage the spending power of those who still have a paycheck.

WEAK SUPPORT. Just as troubling is Zedillo's ability to hold the country together politically: Although he has promised international creditors an austere, orthodox path to economic recovery, opposition parties and labor unions are expected to block proposed privatizations and press for more government spending. "The country is on the verge of economic collapse," says Congressman Adolfo Aguilar Zinser, of the left-leaning Party of the Democratic Revolution. "Zedillo does not have the political support to apply a painful, orthodox program."

Ultimately, Zedillo will have to strike a delicate balance between buying opposition support for his economic program and satisfying members of his own ruling Institutional Revolutionary Party, who are chafing at his attempts to make

Mexico's long-closed political system more democratic. As for the Mexican people, Zedillo now has little to offer but a year of sacrifice.

Although the bailout appears to solve Mexico's short-term financing woes, key sectors show signs of vulnerability. The jump in interest rates sparked a spate of loan defaults that could push the banks' nonperforming loans to as high as 30% of total loans from 8% to 10% now, says David Hale, chief economist at



MEXICAN BOLSA: Financial jitters will create havoc

Kemper Financial Services Inc. Meanwhile, Mexico's three biggest banks—Banamex, Bancomer, and Serfin—owe overseas creditors nearly \$5.5 billion in dollar-denominated certificates of deposit, all of which fall due during the next 90 to 180 days. The banks say they're liquid enough to pay off the notes, but sharply higher domestic loan defaults eventually could make that difficult. Major corporate borrowers, holding some \$3 billion in international commercial paper, also will be hard-pressed to make payments.

In the months ahead, consumer spending on everything from household appliances to automobiles is expected to drop 30% to 50%. Mercedes-Benz, Ford, Nissan, and Volkswagen all have carried out

plant shutdowns, with more to come. Construction will be hit hard, too. The government's emergency economic program includes big cuts in infrastructure spending, and high interest rates have put most private projects on hold. ICA, Mexico's largest construction company, hopes to go ahead with a \$100 million Mexico City development. But Paul Reichmann and George Soros, ICA official Eduardo Borja admits affordable financing will be tough to find: "The project is still viable, but the financial crisis has put the brakes on."

Exporters, certainly, will gain from the cheaper peso. Tilemaker Intercontinental de Cerámica plans to sell 50% of its production to the U.S. and Canada up from 40% last year. Exports of canned processed foods and beer will do well. And makers of tires and textiles, which had been hurt by the

Where Mexico Will Suffer Most

BANKING High interest rates will cripple many corporate customers, driving up nonperforming loans to as much as 30% of lenders' portfolios

CAPITAL GOODS Sales of everything from cars to washing machines are expected to drop 30% to 50% as consumer credit costs soar

CONSTRUCTION Drastic government infrastructure spending cuts, and a slowdown in office building, will force a major slump

CONSUMER PRODUCTS A 7% cut in salaries, combined with inflation of 25% to 40%, will dampen demand, especially for imports

imports, will benefit from diminished competition from overseas. A sharp drop in imports from the U.S., combined with greater Mexican exports, is expected to help quickly reduce Mexico's \$28 billion current-account deficit—one of the factors that triggered the peso devaluation.

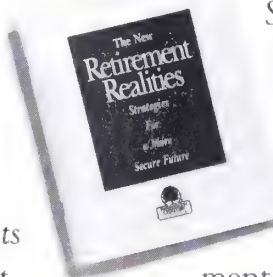
Indeed, export strength likely will be a boon to *maquiladoras*, plants along the U.S. border that produce large quantities for foreign markets. Samsung Electronics is going ahead with a \$500 million investment in a Tijuana plant. But electronics producers who also had been targeting the Mexican market have put growth plans on hold. Sony Electronics de México General Director Koichi Namura expects that domestic demand

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From A. Gary Shilling & Co., Inc. (Springfield, NJ), 1994 Long Term Forecast, October 13, 1994

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for audio and video equipment will drop 30% to 40% this year. "The market is shrinking drastically," he says. "People... don't need a TV set right now."

Similarly, many of Mexico's small, family-run companies will struggle. José Guaidá's family makes plastic tricycles and beach toys. Most of their materials—plastic and steel—are imported, and Guaidá is allowed to pass on just

30% of price increases to customers. To boost volume in the face of shrinking margins, Guaidá is expanding his line of beach toys, figuring that more Mexicans will spend vacations at the beach close to home. "We've survived devaluations before," says Guaidá with a shrug. "It's better to keep working."

Zedillo is counting on such common-sense support as he attempts to shep-

herd the economy through the coming months. To succeed, though, he must cater to two very different constituencies: impatient Mexicans eager to get their long-postponed share of prosperity and foreign investors who, like him, not now have a great stake in seeing that Mexico reaches its goals.

By Geri Smith, with Elisabeth A. Kin, in Mexico City

COMMENTARY

By William Glasgall

WELCOME TO THE NEW WORLD ORDER OF FINANCE

Global financial panics erupt every decade or so. But even by historical standards, Mexico's currency collapse ranks among the scariest. With the crisis stretching into its seventh week, investors were stampeding. Worse yet, the panic was spreading from Buenos Aires to Budapest. Even the dollar was taking an unexpected shellacking. Some were bracing for another 1987 crash—not just in Mexico City, but in New York, London, and Tokyo.

It took forceful action to stop the runaway markets before they dragged the world economy down with them: \$49.8 billion in loans and guarantees for Mexico from the U.S. and its allies. Some bankers say the total could reach \$53 billion or more. Certainly, this will go down as the largest socialization of market risk in international history.

AMBITIOUS LABOR. With the U.S. spreading the gospel of democracy and free-market economics throughout the developing world, Clinton and his cohorts had little choice but to assemble the megaplan. As the club of emerging-market nations expands, the rich nations' obligation to provide a safety net for poorer trading partners is growing exponentially. America and its allies must mount a collective drive to ensure global monetary and economic stability—much like their efforts to maintain geopolitical order in the post-cold-war era.

Such ambitious labor is needed because the nature of financial markets

has changed since Latin America's last financial crisis in 1982. Back then, it was gunslinging bankers who lent to Latin America. Because banks could lend for the long haul and absorb losses, they were a valuable shock absorber for the financial system. When enough Latin loans eventually went bad, it still took years to

leaders should be able to act with similar speed.

Clinton's \$40 billion in loan guarantees for Mexico got nowhere because Congress objected to bailing out Wall Street. Legislators also did not like the U.S. shouldering most of the cost. They were right. Emerging markets will stay volatile, and countries and investors shouldn't expect a handout every time an economy hits a rough patch. And when a rescue is necessary, it should be global.

BRIDGE THE GAP. Europe and Japan, after all, will benefit from a healthy Mexican economy and thus should bear the burden of supporting it in times of crisis. Likewise, Washington should be obliged to lend a hand to European or Asian allies if Poland or Indonesia comes unglued. One way to keep the next crisis at bay: bridge the gap between short-term money and long-term investment needs.

In addition, emerging economies need to take steps to immunize themselves from the vagaries of a fund-dominated world. It would help a lot if more of them developed mandatory pension schemes to build up domestic savings. Along with that should come privatization. With capital so flighty, it may take hard decisions to make money stay put. But if the first world wants to encourage capitalism, it will have to underwrite it—even if the cost is huge.

William Glasgall is a Senior Writer specializing in global finance.



craft and conclude their restructuring.

Since then, bankers have wised up. Now, others with a shorter time horizon make the emerging-market deals. This time, it was mutual-, hedge-, and pension-fund gunslingers who provided the capital. Mexico attracted \$45 billion in mutual-fund cash in the past three years. And when the peso dived, fund managers bolted. In this global market, all it takes is a phone call to Fidelity to send money hurtling toward Monterrey—or zooming back. And world

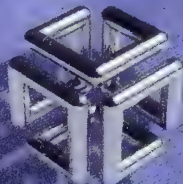
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AUTOS

HALFWAY UP THE HILL AT GM

One good quarter does not a turnaround make

Was that a sigh of relief coming from G. Richard Wagoner Jr.'s office on Jan. 31?

That morning, General Motors Corp. reported that its core North American auto operations (NAO), which Wagoner has headed for barely six months, made \$690 million. It was the unit's first profit since 1989 and a far cry from the anemic third-quarter results that Wall Street greeted in October by pounding GM shares down 12%. This time, GM's stock jumped 1½, to \$38. "We celebrated here this morning for five minutes," says Wagoner. "Now it's back to the salt mines."

That's just as well: NAO, GM's problem child, still has a long road to real recovery. Its 0.7% net profit margin of last quarter seems absurdly low compared to Wagoner's goal of 5%—a target he concedes will be tough to hit before the next recession. Meanwhile, GM must scramble to erase its pension-fund shortfall, restore its sunken credit rating, renew its aging product lineup, and dramatically lift productivity. One extra complication: The United Auto Workers likely will continue to pepper NAO with work stoppages. Says PaineWebber Inc. analyst Stephen J. Girsky: "At General Motors, it's a race against time."

"SMOOTH SAILING?" In the year ahead, though, Wagoner is likely to start seeing considerably higher profits at NAO. After putting one-sixth of factory capacity through lengthy model changeovers and other major renovations last year, the unit now has little downtime scheduled. That means more output, higher productivity, and less costly overtime and premium freight expense. "It should be smooth sailing at NAO for at least the first half of the year, barring labor interruptions," says Wertheim Schroeder

& Co. analyst John A. Casesa, who expects NAO to earn \$2.85 billion this year.

GM's latest financial results, which exceeded analysts' expectations, provide further encouragement. NAO's fourth-quarter revenue-per-vehicle jumped nearly \$1,100 from a year earlier, to \$18,176, Girsky figures. One

reason: NAO is building more high-margin trucks, up to 40% of total units from 38%, though still lagging the industry's 44% average. And NAO has fattened its bottom line by curbing low-profit sales to rental-car fleets and by trimming rebates and other marketing incentives.

GM's results still pale next to Ford Motor Co., which on Feb. 1 reported that its fourth-quarter U.S. auto profits had doubled, to \$3 billion. But GM may gain some competitive advantage from the economy. The Federal Reserve's series of interest-rate hikes appears to be cooling off red-hot auto sales. If that brings a longer, flatter sales plateau, GM will have more time to cut costs and clean up its balance sheet. The nagging fear, of course, is that the Fed could actually choke off the recovery. Indeed,

slower January sales have raised fears that the auto sales boom may be waning before most analysts expected. "The big gorilla for GM is still the [economic] cycle," says analyst John V. Kirnan, of Salomon Brothers Inc.

Boom or no, Wagoner must prove he can lick NAO's persistent problems. Strikes have crippled output six times



WAGONER: "We celebrated for five minutes"

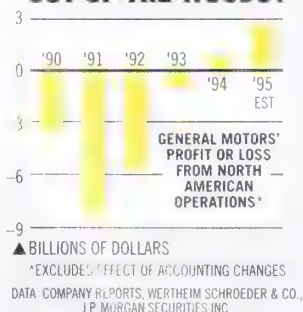
since the beginning of 1994, and the new NAO chief hasn't yet shown he can placate GM's contentious rank and file. And NAO's launches of crucial vehicles such as Chevrolet's Lumina family sedan and Cavalier compact have been plagued with costly delays. As a result, GM's ready anemic share of the U.S. light-vehicle market edged down three-tenths of a point to 32.9% last year. And NAO missed its goal of a 9% gain in manufacturing productivity, improving only 5% for the year.

STILL SLOW. Such is the challenge Wagoner, 41. He was a star in GM's New York treasurer's office, where he was hired in 1977. Named NAO's chief financial officer in 1992 after a string of overseas postings, he won GM credibility adopting more conservative financial methods. Within NAO, the unpretentious straight-talking executive is well regarded, though griping persists about his relative youth and lack of engineering or manufacturing experience. Already, he has reshuffled top management and combined four car groups into two, yoking Saturn closer to other units.

Wagoner's main frustration, says one GM insider: "Nothing is happening as fast as he'd like it to." GM's North American unit remains an unwieldy slow-changing elephant. Enough with the champagne. Back to the salt mines.

By Kathleen Kerwin in Detroit

OUT OF THE WOODS?



GM is scrambling to renew its aging product lineup and improve productivity before the next downturn

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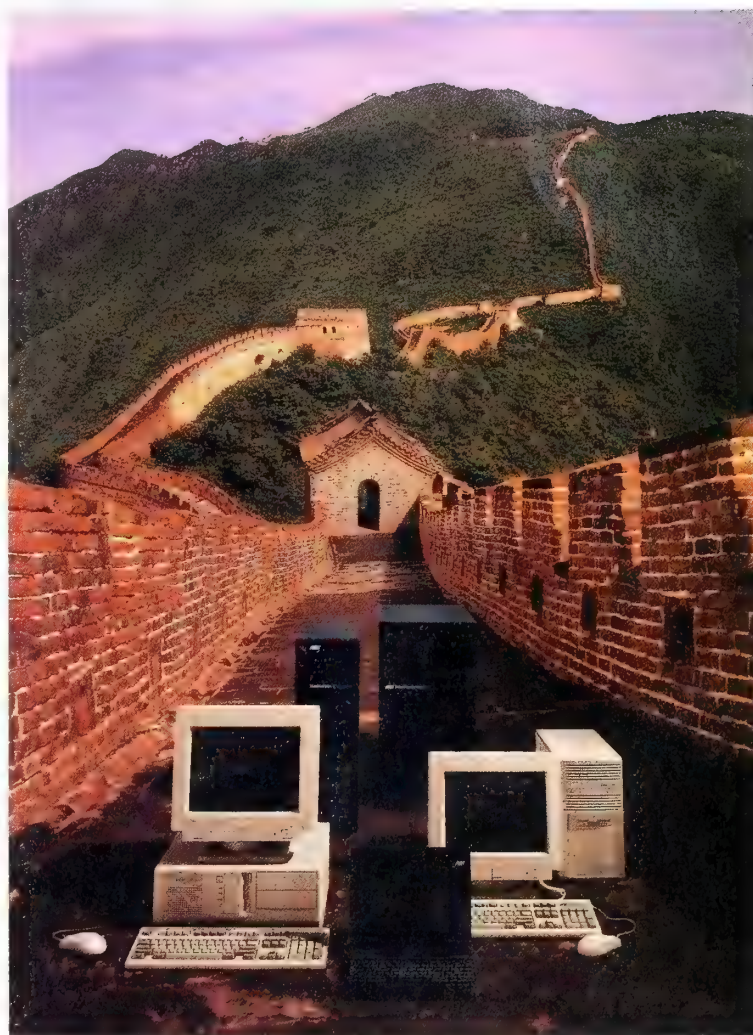
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COMMENTARY

By Aaron Bernstein

WHY LANE KIRKLAND LOOKS LIKE A LAME DUCK

The whispers are back. Since the Republicans swept into power in Congress last November, there have been rumblings in the union halls and in the corridors of the AFL-CIO. At the federation's executive council meeting in mid-February, the question will come up again: Is it time for President Lane Kirkland to retire?

Such sniping has cropped up before during Kirkland's 15 years atop the federation—but never so publicly or widely. Unionists are deeply frustrated, and they should be. After a decade in which unions suffered a near-death experience, Kirkland acts as though little has changed.

NO FIREBRAND. True, the decline of unionism can't be ascribed to lackluster leadership. Heightened management antipathy, America's broad shift out of manufacturing, and the rise of the global economy have done more to reduce membership. And Kirkland, who declined to comment, didn't lose the November elections. But the federation president's strategy to combat those long-term forces hasn't worked. Kirkland waited 12 years for a Democratic President who could save unions, then watched as the Clinton Administration failed to deliver on labor's requests. Now that the GOP runs Congress, Kirkland seems to have no other plan for reviving the movement.

More than that, the crusty 72-year-old presents a condescending public image that reinforces the image of labor unions as out of touch with the workers. More intellectual than firebrand, he shuns TV interviews and speaks in endless Proustian sentences. Says Ron Carey, president of the International Brotherhood of Teamsters, the federation's largest union: "We need a labor movement that has some fire in it again, and that means a change at the top."

Carey and others complain that Kirkland has lost his relevance. A



UNFOCUSED: Kirkland lacks a plan to revive unions

card-carrying cold warrior who has devoted much of his lengthy career to battling communism, Kirkland spends one-third of the AFL-CIO's \$100 million annual budget on four foreign affairs institutes that support overseas labor unions. He seems less interested in the plight of American unions. "He spends an extraordinary amount of time dealing with Eastern Europe while we're going to hell in a handbasket," complains Robert E. Wages, president of the Oil, Chemical & Atomic Workers International Union.

Indeed, it's often difficult to tell what the federation's domestic strategy is. The labor movement split into two schools in the 1980s. One sought cooperation with management to help fend off global competition; the other attacked employers for demanding employee concessions. Kirkland advocates neither view and has no alternative. Instead, he resisted the cooperation way of thinking for a decade, then finally allowed AFL-CIO Secretary-Treasurer Thomas R. Donahue to spearhead a committee that endorsed the concept last year.

Kirkland's biggest achievement in that time: bringing the auto workers, mine workers, and Teamsters back into the

AFL-CIO. This strengthened the federation but didn't lift overall union membership. Meanwhile, opportunities have gone unexploited. Many workers are anxious about falling wages and lost jobs, yet the loudest voice on the subject is a government official, Labor Secretary Robert B. Reich. What's more, numerous surveys indicate that about 40% of all workers would like to join a union, far more than the 16% that actually belong (chart). Kirkland has done little to make Americans aware of the dramatic

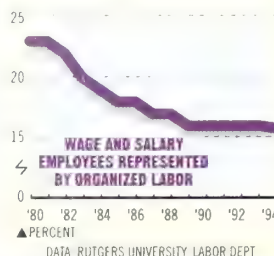
increase in illegal firings of union supporters that dampen organizing drives.

NEW LEADER? Some unionists think Kirkland should retire when his term ends in October and let Donahue take over the ship. Even some stalwart supporters now seem open to change. "I'm 100% behind Lane until there's another candidate, and then I'll take a look at all the candidates," says Albert Shanker, a friend and longtime supporter of Kirkland's who heads the American Federation of Teachers.

It's not clear yet whether the federation's 86 unions will screw up the courage to act on their complaints. If they do, Donahue likely would serve as president for one or two two-year terms. A new secretary-treasurer, poised to take charge for the longer term, might be a younger leader such as United Mine Workers President Richard L. Trumka. One of labor's best stump speakers and just 45 years old, Trumka could help rejuvenate labor's image. No one will singlehandedly restore the labor movement's preeminence. But someone like Trumka just might help return it to relevance.

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STRATEGIES

FIDELITY'S NEW CONTRACT WITH AMERICA

Steffanci's ouster signals a conservative shift

As head of Fidelity Investments' bond operations, Thomas J. Steffanci produced a profoundly enviable record. In just five years, he built a business with 63 funds and \$27 billion in assets. His funds outperformed their industry peers each year until 1994—and even then, returns were only slightly below average. “If last year was a disaster, a lot of fund groups have disasters every year,” says John Rekenhthal, editor of *Morningstar Mutual Funds*.

Within Fidelity, though, 1994 was indeed seen as disastrous. Aggressive investments by some of Steffanci's managers, combined with rising interest rates, produced lousy results at key funds. Most embarrassing were hits to the firm's most conservative short-term funds—the vehicles investors count on never to lose money. Shareholders pulled out hundreds of millions of dollars.

REINED IN. In late January, Fidelity acted to prevent such surprises again, announcing Steffanci's resignation and the reorganization of his bond operations under J. Gary Burkhead, Fidelity's chief of investments. Five fund managers were reassigned; separately, emerging-markets specialist Robert Citrone left to join hedge fund Tiger Asset Management. The moves signaled an attempt to

curb Fidelity's conservative funds, which under Steffanci had tried to juice yields by taking risky bets in emerging-market debt. Says an insider, “the funds that strayed will get pulled back in.” Steffanci wouldn't comment.

The moves may finally soothe investors, who pulled \$800 million from Fidelity's bond funds in December and \$100 million more in January. But now, Fidelity must grapple with an issue facing many funds in the wake of last year's historic bond-market debacle: How can it balance performance with conservatism? Burkhead's reorganization, say insiders, was aimed at instilling some caution into the bond group's high-octane investment culture. But if Fidelity pulls back too hard, shareholders could suffer. “If they go too conserva-



THOMAS STEFFANCI

JUST TOO AGGRESSIVE? Bond-fund investors have pulled out in droves

tive, they're less likely to recoup” loss says Sheldon Jacobs, editor of the *Load Investor* newsletter.

Steffanci had created a fiercely aggressive corps of fund managers, buying teams of specialists in derivative and emerging-market debt. Managers encouraged to think like stockpickers could double their salaries if their funds performed. The approach encouraged risk-taking that appeared, at times, inappropriate. Fidelity was stunned when one of its most conservative products, the Short-Term Bond fund, lost 4.1% last year—worse than three-quarters of similar competing funds (page 94). Investors pulled out in droves, with assets

plummeting more than 40% to \$1.5 billion. The reason: manager Donald G. Taylor, who had been investing heavily abroad, was burned by a hefty stake in Mexico. Another big fund managed by Taylor, Spartan Short-Term Income, fell 4.6% and assets dropped to \$600 million from \$1.5 billion.

Numbers like those got attention fast—hence Burkhead's intervention. I wouldn't comment, but investors say he wants to establish

a clear line between Fidelity's conservative funds and its high-risk funds.

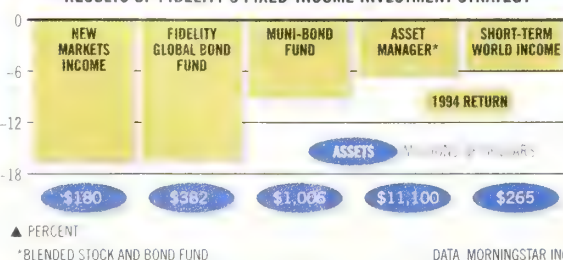
NO HOTDOGGING. That's probably why Taylor, for one, has been reassigned more aggressive vehicles. Following Citrone's departure, the emerging-markets group has been placed under junk-bond chief Robert Lawrence, indicating that Fidelity will significantly pare back investments in those markets. The first change: Robert A. Beckwitt, the star manager of Fidelity's \$11.1 billion Asset Manager fund, will leave the bond group to join the equity group. Beckwitt says his investment strategy won't change. Taylor wouldn't comment.

Some question whether Burkhead is going far enough. One possible problem: The bond group's compensation system, which remains unchanged, generates handsome annual performance bonuses without accounting for risk. Even so, Fidelity has made its message perfectly clear: After losing 11% of its bond-fund assets, the firm wants to keep hotdogging in check. Risk has its place—but it's not in conservative investments.

By Geoffrey Smith in Boston

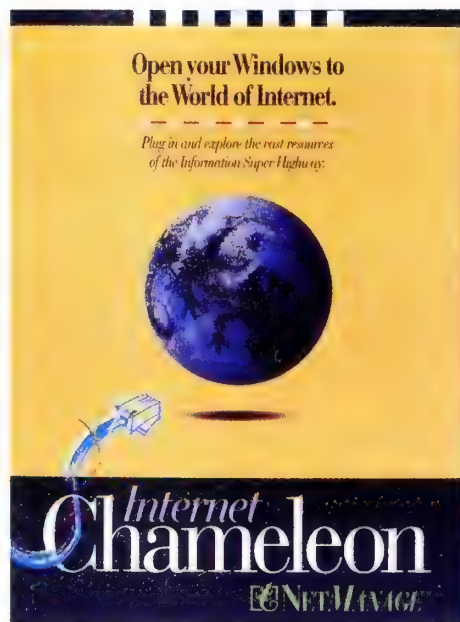
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TELEVISION

THE PEACOCK STRUTS ITS STUFF

NBC still has a way to go, but it's scoring key ratings victories

It's rerun time. A decade ago, Bill Cosby led a woeful NBC Inc. to ratings nirvana. Today, instead of the family-friendly Cos, it's the endless stream of drug overdoses and accident victims being wheeled through *ER* that has hearts throbbing at NBC's parent, General Electric Co.

Before the Jan. 29 mega-ratings for the Super Bowl bolstered ABC's lead, NBC had mounted the kind of rally the San Diego Chargers couldn't muster. Third last season, the Peacock network has a powerhouse Thursday-night lineup of *Seinfeld*, *Mad About You*, and *ER* that has propelled it to three straight ratings victories in the 18-to-54 age group for the first time since 1992. And there's good a.m. news, too: *Today* regularly wins the morning-show race.

"REAL HORSE RACE." With its early season lead, ABC still expects to win the year's prime-time title. But even when counting the Super Bowl's 120 million viewers, ratings at the Capital Cities/ABC Inc. unit are down 3% from last year, according to Nielsen Media Research. That sets up 1995-96 "as a real horse race between ABC and NBC," says media buyer Paul Schulman.

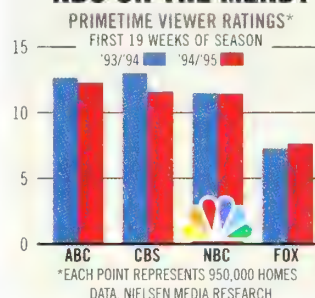
So far, NBC's strength hangs mainly on one blockbuster night. Mixing upscale comedy and fast-forward medical action has attracted one of every three TV sets turned on during Thursday prime time.

Such success is a remarkable reversal from 1993, when NBC had lost a third of its viewers over three years.

Gone was *The Cosby Show*, L. A. Law was fading, and *Seinfeld* had just a small audience on Wednesdays. Programming boss Warren Littlefield's job was on the line, and Don Ohlmeyer was brought in as entertainment chief to help turn things around.

And turn they did. NBC has added such hits as *Frasier* and *Friends*. And it signed Steven Spielberg to make *ER*. It also gambled mightily by sending *Frasier* to Tuesday night up against the top-ranked *Home Improvement*. To Madi-

NBC ON THE MEND?



son Avenue's surprise, *Frasier* proved stout competitor: Ranked 14th for the year, it has helped close the Tuesday-night gap. Securer in his job and emboldened by success, Littlefield may shift other Thursday-night standouts to weaker lineups.

BOWL HOPES. Beyond its programming, NBC is closing the prime-time gap thanks to gains by the Fox network, largely at the expense of ABC and CBS.

The 20-something drama *Melrose Place* and the supernatural thriller *X-Files* have helped boost Fox's ratings from last year.

But the champ is worried about being dethroned—yet. With *Home Improvement*, *Roseanne*, and *Gun Under Fire*, ABC is the team to beat. E

NBC has momentum and it gets to air the Super Bowl next year. That could be the Hail Mary pass that gives the No. 3 network a come-from-behind victory.

By Ronald Grover in Los Angeles

PENSION FUNDS

THIS GADFLY IS REALLY BUZZING

CalPERS is issuing fresh reprimands to laggard boards

The dreaded list is back. On Feb. 2, the \$80 billion California Public Employees' Retirement System planned to release its annual catalog of crummy companies—a distinction based on stock performances and the fund's complaints about management. "We view this as a wake-up call," says CalPERS General Counsel Richard H. Koppes.

The 1995 list is comprised of nine companies, which rank among the worst-performing stocks in the pension fund's portfolio of 1,200 companies. Other factors that can land a corporation on the spot: unresponsiveness to CalPERS inquiries, labor practices, and the percentage of shares owned by CalPERS. This year, the unfortunate nine included

se Cascade Corp.—a four-time offender—and Navistar International p., which has made the list two rs running. Others, such as golf-club er Zurn Industries Inc. and oil and producer Oryx Energy Co., are less iliar (table).

KE-UP CALL. With the list, CalPERS es to persuade corporate boards to e management and strategic chang- inside its targeted companies. To- d that end, the pension fund has in- d itself to meetings at companies to l management and directors. And t of this year's offenders are cooper- g with the pension fund—possibly ause it's the fastest way off the list. ne emphasize, however, that they t make changes simply because PERS wants them to do so. "No deci- was driven singly by CalPERS," says e's director of investor relations. hould any of the companies on the PERS list fail to make significant al- ations, Koppes promises that he t hesitate to turn up the heat, as he done in the past. "Filing a share- er proposal is the buzzer for heavy pers," says Koppes. Given CalPERS' it, few corporate boards that made 1995 list will want to risk the fund's cial brand of shock therapy.

By Eric Schine in Los Angeles

CALPERS' NAUGHTY NINE

DISE CASCADE The CEO is one, but CalPERS wants more. It says higher paper prices will help.

MART After its stock price lan- ished for years, Kmart split the EO and chairman jobs.

ELVILLE CalPERS is unhappy th the retailer's diversified lines. has met with CalPERS.

AVISTAR Chairman's exit should elp get Navistar off the '96 list. s responding to concerns.

S. SHOE Board has not signed f on annual elections, and alPERS says stock is too low.

IRST MISSISSIPPI Company is en as unfocused. It says it will view CalPERS' complaints.

OSTENS It says shuffling execs d cutting costs have helped, but will meet with CalPERS.

RYX ENERGY Its stock price has unged 80% since 1990. Oryx ys it is trying to improve.

URN INDUSTRIES Maker of gen- erators and golf clubs saw sales ll 50%. It will meet with CalPERS.

WHY VANGUARD'S MONEY MARKET YIELDS HAVE BEEN CONSISTENTLY HIGHER MONTH AFTER MONTH



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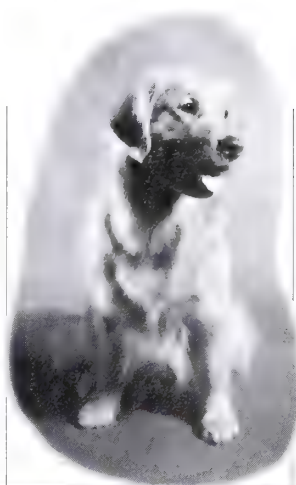
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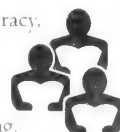
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EDITED BY KEITH H. HAMMONDS

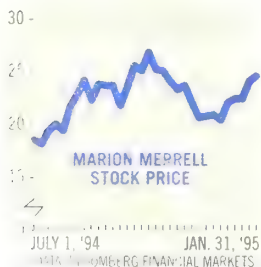
END OF THE LINE FOR UNION PACIFIC'S BID

UNION PACIFIC WALKED AWAY from its four-month-long exercise in acquisition futility—but not before making Santa Fe Pacific shareholders considerably wealthier. UP gave up its battle on Jan. 31 to derail Burlington Northern's proposed acquisition of Santa Fe. The price just got too high, says UP Chairman Drew Lewis. But thanks to UP's intervention, Burlington Northern now will pay \$4 billion in cash and stock for Santa Fe, up almost 50% from its original \$2.7 billion all-stock offer—which Santa Fe's board of directors had

CLOSING BELL

MARION MURMURS

Marion Merrell Dow's stock, long juiced by takeover talk, is up anew on rumors that Hoechst is circling. What could Hoechst want? With patents expired on its Cardizem CD and Seldane-D drugs and with sales of its Nicoderm patch weak, Marion's profits should be \$319 million in 1996, down 54% from 1992, says A.G. Edwards analyst Ken Nover. But Hoechst may see an inroad into managed care. Marion has earned a loyal following of HMO pharmacists, and its Rugby generic drug unit is strong. Nover says Marion may fetch \$28 a share. Hoechst wouldn't comment.



O.K.'d. The richer deal is expected to be approved by Santa Fe shareholders on Feb. 7.

THE ROCKY HORROR AIRPORT OPENING

AFTER FOUR POSTPONEMENTS and countless talk-show jokes, Denver International Airport is set to open on Feb. 28—16 months late and, at \$4.2 billion, twice the projected cost. The infamous automated baggage system, which tended to chew up suitbags, is partly working. But the airport will charge airlines \$18 per passenger to recoup costs, forcing United Airlines and others to add \$20 per ticket. Denverites, promised once upon a time that they wouldn't have to underwrite construction, are furious. Says Colorado Governor Roy Romer, who stumped hard for the new airport: "Had somebody told me that the per-passenger cost was going to be \$18, I would not have supported the airport." Ah, hindsight.

L.A. GEAR AND RYKA TIE THE KNOT

BASKETBALL SHOES WITH light-emitting diodes meet social activism: Sense a disaster in the making? Trendy athletic shoemaker L.A. Gear announced on Jan. 30 that it would acquire Ryka, a tiny maker of high-performance footwear for women. Ryka is known for ads that combine a workout message with calls to end domestic violence. L.A. Gear, which posted a loss of \$22 million last year, is known for earnings troubles. Still, it will pay about \$16 million for the company, plus warrants for Ryka's shares. L.A. Gear said Ryka would be the first of many purchases and licensing arrangements aimed at expanding into the upscale women's and children's sneaker market.

HEADLINER: HOWARD STERN

HOW ABOUT THE JERSEY STERNAPIKE?

Vince Lombardi. Molly Pitcher. James Fenimore Cooper. Howard Stern? In coming weeks, the radio shock jock was to join a pantheon of New Jersey luminaries who have highway rest areas named after them. The Howard Stern Rest Stop off Interstate 295 near Trenton, complete with plaque, would fulfill a pledge from Governor Christine Todd Whitman, in gratitude for Stern's very vocal support.

Now, the National Organization for Women in New Jersey has asked Whitman to reconsider. "Inappropriate and coun-

terproductive," New Jersey NOW President Myra Terry wrote the governor citing Stern's attacks on, well, everyone. "The man is very vulgar," says Roosevelt Nesmith, coordinator for the southern region of New Jersey NAACP branches.

Whitman plans to proceed with the dedication. And the rift has given Stern plenty of fodder. "Why would anyone complain about something so ingenuous and frivolous as this?" asks Stern's agent, Don Buchwald. And why risk the inevitable radio rejoinder?

By Amey Ston



A CANCER COALITION GOES COURTING

THEY COULD BE THE DINOSAURS of health care. Big academic medical centers, with their hefty research budgets and spendthrift ways, seem like candidates for extinction in an era of cost-conscious managed care. Hence the National Comprehensive Cancer Network, a consortium announced on Jan. 31 by 13 cancer-treatment centers. The NCCN will pitch itself to large employers and insurers as a coordinated cancer-care system with national coverage. So far, Tenneco, General Electric, and AT&T show interest.

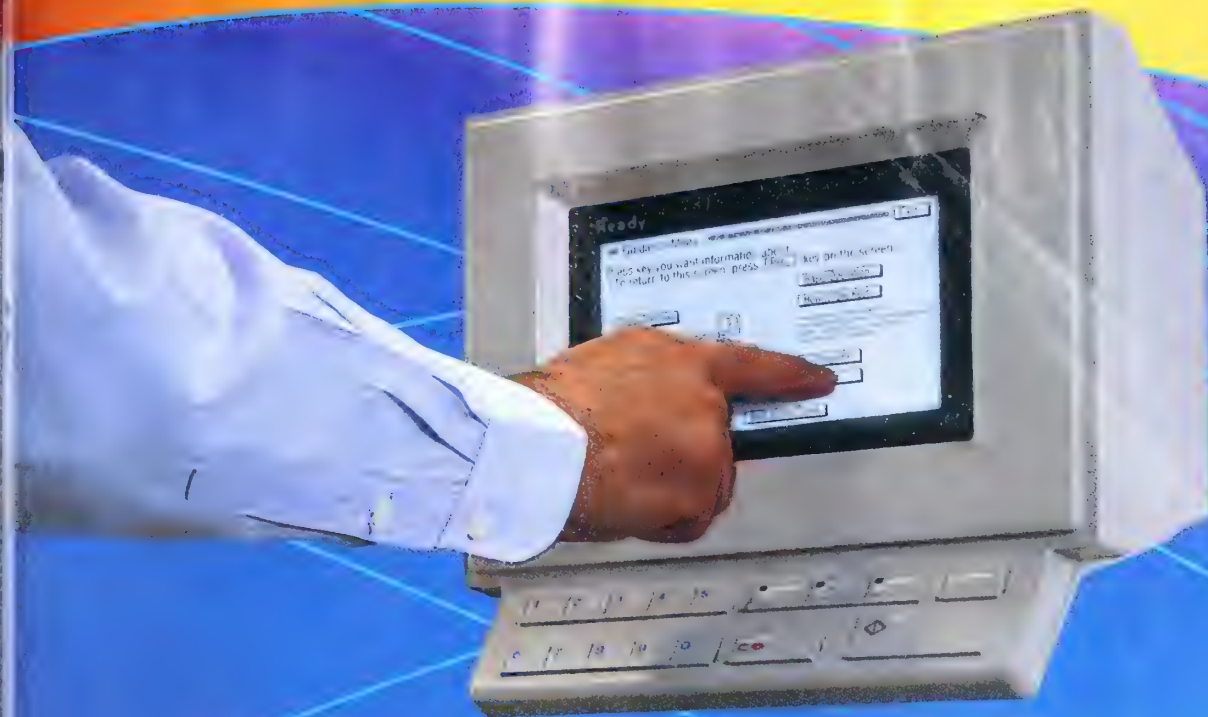
ANOTHER CHOP AT THE CLIPPER CHIP

LIFE GETS HARDER FOR GOVERNMENT electronic eavesdroppers. On Jan. 31, AT&T and chipmaker VLSI Technology

announced a communication system so secure even the National Security Agency supercomputers probably can't unscramble it without battle. The NSA, FBI, and other agencies would much prefer companies to use the so-called Clipper chip, whose "back door" lets them relay messages between suspected terrorists or crooks if they get a court order. AT&T says it will sell Clipper-based systems to anyone who wants them. But few customers

ET CETERA...

- Eastman Kodak took a \$2 million charge to restructure again, cutting 3,200 more jobs.
- Chiat/Day, of Energizer Bunny fame, will merge in Omnicom's TBWA ad agency.
- Samsung countersued Nintendo over allegedly counterfeit video game chips.
- The new honcho at Ben Jerry's: Robert Holland, consultant and erstwhile poet



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THE RULE BOOK FOR BUSINESS ABOUT TO GET SMALLER

Forget the frenzy over the balanced-budget amendment and a capital-gains tax cut. Corporate America is more interested in a quieter Capitol Hill-White House struggle over ways to ease the regulatory pinch on business.

Although the anti-regulation drive hasn't garnered the lines of other GOP crusades, the fight is falling into a familiar pattern: Republicans are leading the charge for sweeping change, while defensive Democrats are revving up their package to stay in the game. The result: a win-win situation for Washington's business lobbyists.

Insisting that regulations are choking industry, the GOP has reprised a favorite defense—the regulatory freeze. Republicans are shooting for a late February House vote on a six-month moratorium that would suspend nearly all new rules. Among the targets are proposals business opposes, such as rules on toxic emissions from hospital incinerators, and some that industry supports, including a seafood inspection program.

PHASES. The furthest-reaching GOP proposal would require stringent scientific studies to weigh risks and gauge the costs and benefits of new rules. And a "regulatory budget" would cap compliance costs for business at 5% of gross domestic product. "Government will have to show a compelling reason to interfere with the market," says Representative David McIntosh (R-Ind.), former head of Vice-President Dan Quayle's Competitiveness Council. The Clinton Administration has come up with a two-phase approach to head off the GOP onslaught. First, Clintonites are lambasting the Republican plan as a radical attempt to gut health and safety rules. If the GOP's scheme had been in effect earlier, "we wouldn't have banned lead in gasoline," says Environmental Protection Agency Chief Carol M. Browner. "A generation of children may have been needlessly brain damaged."

The White House also is trying to dampen business enthusiasm for the GOP blitz by arguing it could lead to cumbersome risk-assessment reviews. New pesticides, for example, might be kept off the market pending fresh studies. "Some of these proposals are calculated only to make the process more complicated and more expensive," says John M. Quinn, Vice-President Al Gore's chief of staff.

But the Clintonites know they can't just cry extremism. So Gore is working on the second phase of the attack: a plan to give industries more flexibility. Current rules often dictate the

equipment companies must use to comply with the law. The Gore initiative would scrap that approach and replace it with broad performance standards that corporations could meet any way they want. Separately, the Veep has ordered agencies to review their rules and junk unnecessary ones. The Hill and the White House "have interpreted the message from the election, and that's 'Get government off our backs,'" says DuPont CEO Edgar S. Woolard Jr.

Trouble is, Gore isn't expected to produce his proposals until spring. And some White House officials concede that may be too late to affect the Hill debate.

The House bill is sure to change as it heads for a vote in late February. Its supporters admit it's flawed. But even the final version may be too radical for the Senate. Senator William V. Roth Jr. (R-Del.) has introduced a measure that would require risk studies on rules that cost more than \$100 million, rather than the House's \$25 million threshold. And Roth's plan doesn't dictate how risk assessments should be conducted, as the House measure does. To business, it doesn't matter which plan prevails. One way or another, regulatory relief is at hand.

By Mary Beth Regan and Susan B. Garland, with John Carey



NET RESULT: No new inspections

CAPITAL WRAPUP

SCIENCE SPENDING

Despite the spending squeeze, science and technology will fare well in President Clinton's fiscal '96 budget. Administration insiders say they will maintain current funding levels or even boost them to demonstrate their commitment to investing in the future. The White House doesn't expect opposition for most science programs. The reason: House Speaker Newt Gingrich (R-Ga.) and House Science Committee Chairman Robert S. Walker (R-Pa.) are technobuffs.

LENDING BIAS

► The battle of the number crunchers continues. In 1992, a Boston Fed review of thousands of mortgage files found a pattern of lending bias against minorities. But a recent Fed study reached a different conclusion. And now a draft report by a Federal Deposit Insurance Corp. economist contends that the 1992 Boston Fed study was flawed. The GOP will use the new reports to rein in the Clintonites' enforcement of fair-lending and community-reinvestment laws.

THE AIRWAVES

► The market for hand-held personal digital assistants such as Apple's Newton could begin to take off this year, thanks to a ruling expected from the Federal Communications Commission on Feb. 7. That's when the agency will set aside a chunk of the airwaves for these gadgets, which now have to be tethered to wires to transmit data. Companies such as IBM plan to use the spectrum to eliminate cumbersome cables that lash together computers in local-area networks.

GERMANY

BONN'S TELECOM BOMBSHELL

Breaking DT's monopoly will have huge repercussions

Wolfgang Bötsch, Germany's Post & Telecommunications Minister, is known in Bonn's corridors of power as a master of political ambiguity, a careful bureaucrat with a gift for the innocuous-seeming sound bite. But his mild public pronouncements—to those shrewd enough to read them carefully—can also signal major policy shifts with big implications for German and European business and the pace of regulatory change on the Continent. It was such an announcement, on Jan. 31, that has Corporate Germany buzzing about the chances of a major speedup in the deregulation of the country's \$66 billion telecommunications market.

Here's what happened. At hearings to consider the best way to update Germany's telecom laws, Bötsch said he would consider permitting limited competition against state-owned phone monopoly Deutsche Telekom well before the 1998 European Union deadline for total deregulation. At the public level, at least, it was a simple move that didn't seem to threaten the status quo.

GREEN LIGHT. But according to industry executives, Bötsch behind closed doors was going much further. By as early as this summer, Bötsch may well be throwing open the door wider than many imagined in several segments of the German phone market. Bötsch, say these insiders, will give the green light to powerful German companies that want to break Telekom's monopoly network.

That would allow companies that offer private corporate networks and other services to bypass Telekom and slash their prices. Now, they must lease costly lines from Deutsche Telekom itself in order to get into the phone business. Bötsch also assured industry leaders that they could soon start challenging Telekom with such high-tech services as multimedia and video-on-demand.

The implications of Bötsch's actions could be far-reaching.

German corporations will experience for the first time the benefits of low-cost, state-of-the-art service. "We'll push for it, and we'll use it," says Gerhard Rist, the executive in charge of telecom services for chemical giant BASF Group. At present, Deutsche Telekom rates can run as much as 300% higher than those in Britain, where the phone market has already been deregulated.

Big German companies are eager to take on Deutsche Telekom. Energy utility Viag, which now has 4,000 kilometers of fiber-optic network, hopes to wire the cities of Munich and Nürnberg. Veba, another energy company, is teaming

up with Britain's Cable & Wireless PLC. It already has its own fiber-optic network, which it is seeking to offer to such third parties as corporate network operators at rates as much as two-thirds lower than existing Telekom prices. Veba board member Hermann Krämer says he already has one major customer who will lease capacity on Veba's network to the tune of more than \$65 million a year.

BIG CHANGES IN GERMAN TELECOM

How deregulation will look

NEW VENTURES.

Partnerships between German companies and foreign telephone companies are gearing up to offer alternative telecom services to corporations, universities, and cities

NEW NETWORKS.

Instead of leasing costly lines from Deutsche Telekom, the new ventures will seek to operate their own lower-cost fiber-optic networks

MORE COMPETITION.

The joint ventures will increase the pressure for further market openings before the European Union deadline of 1998

DATA BUSINESS WEEK



Steelmaker Thyssen, for its part, teamed up with BellSouth Corp. Herbert Brenke, chief executive of E-Mobilfunk, a cellular-telephone operator, figures if he can cut out the use of Telekom lines to his switching station, he should be able to reduce fees by at least 50%.

CHAIN REACTION. The emergence of greater competition in the corporate sector could start a chain reaction throughout Germany that accelerates the whole process of opening markets Europewide. "Once there's a crack in the wall, you can't control it anymore," says Candace Johnson, founder of a private telecommunications trade association in Bonn and vice-president of Inetium, the global satellite-services company. France, Italy, and Spain could feel pressure to speed up their own planned deregulations.

There's no doubt, as Bötsch told BUSINESS WEEK, that "the climate for liberalization has substantially improved." Still, deregulation remains political dynamite in Germany. Deregulation will force a radical restructuring at Deutsche Telekom, which already plans to eliminate 50,000 of its 230,000 workers by the year 2000 to become cost-efficient. Quicker deregulation might generate more job losses.

WILL GERMAN LABOR BE THE FIRST TO BLINK?

Unions are talking tough, but employers intend to stand firm

Porsche, the luxury sports-car maker, has fought hard for three years to slash large losses, with measures from layoffs to lean production. Now, with sales up 23%, to \$790 million in the first half of fiscal 1995, CEO Wendelin Wiedeking told the company's Jan. 27 annual meeting that breakeven is within sight. But three days later, workers at Porsche plants near Stuttgart walked off the job for half an hour.

It's showdown time in labor negotiations in Germany. The guerrilla-style "warning strikes" against Porsche and dozens of other industrial companies are a tactic by Germany's largest labor union, IG Metall, to back its demands for 6% wage hikes, shorter work weeks, and extra Christmas bonuses for its 3 million members. But though IG Metall officials are talking tough, companies seem well positioned to resist. Labor-market analysts expect them to hold wage increases to around 3%, just a smidgen above the current inflation rate.

TIGHT SQUEEZE. That's crucial for Germany's recovery. Led by exports, the economy appears headed for a solid 3% growth in gross domestic product this year. But hefty wage raises now would prompt the Bundesbank to hike its 4.5% discount rate, putting the economic upswing in danger. Contract negotiations this year for an additional 7 million workers will be patterned on IG Metall's.

Union leaders are in a squeeze. They need to sound militant to workers in order to gain recruits. Since 1991, the 16

big unions grouped in the Deutscher Gewerkschaftsbund (DGB) have lost 17% of their total membership. But union officials also know that overblown wage demands will price more jobs out of existence. With unemployment now 3.6 million, or 9.9% of the workforce, that's a powerful motive for labor moderation.

A lot of union taboos are dropping. In Jan. 25 discussions with employer and government representatives, DGB leader Dieter Schulte offered major concessions. He was ready, for instance, to talk about four-day weeks at lower pay and Saturday work without overtime premiums—a pattern set by Volkswagen. But employers are unwilling to give the job guarantees that unions want.

While trying to sound combative to their rank and file, union leaders are arguing to employers that their demands are modest compared with workers' real income losses over the past three years, including bigger social-security and income-tax bites.

Employers feel just as overburdened. They will fight hard to hang on to the double-digit gains in productivity they made last year. At stake for companies such as Porsche is the payoff from restructuring undertaken to survive in world markets. Insists Heinrich von Pierer, CEO of electronics giant Siemens: "We cannot pass on [as wage hikes] the full amount of productivity increases."

Amidst fierce global competition, the costly German mark, up 14% against the dollar since the end of 1993, is a

severe price handicap for German producers. "In many ways, Germany remains a highly uncompetitive place," warns London-based Morgan Stanley & Co. economist Brian V. Mullaney.

That worry is keeping a rein on German union demands as the economy turns up. Labor's restraint is leaving room for employers, particularly companies producing for export, to earn higher profits. It is Germany's best hope for success in its competitive makeover.

By John Templeman
in Bonn

A PHONE EXCHANGE IN MANNHEIM: GERMANY IS HEADED FOR FULL DEREGULATION BEFORE THE 1998 DEADLINE

Given this volatile mix of politics and business, it comes as no surprise that in the past few months regulators and executives have been battling over course of Germany's telecommunications policy. Outside pressure has come from the U.S. Federal Communications Commission, which has threatened to block a \$4.2 billion investment by Deutsche Telekom and once Telecom in Sprint Corp. unless deregulation in the telecoms' home markets is accelerated. "Germany is a key market in Europe in telecommunications," suggests FCC Chairman E. Hundt. "They have got to go faster to get to the same conditions that characterize our communications market."

Bötsch responded to all his pressures Jan. 31 with his private signal that would pry open the corporate market. To defend himself against the labor unions and the German left, which are opposing deregulation, Bötsch can still claim he has preserved Deutsche Telekom's voice monopoly. But the market forces he has unleashed may yet return his well-laid plans.

By Gail Edmondson in Paris, Karen Wry Miller in Bonn, Julia Flynn in London, and Mark Lewyn in Washington



CRUNCH TIME: IG Metall wants 6% wage hikes

SUMITOMO BIT THE BULLET. WHO'S NEXT?



JAPAN

AN \$8 BILLION WRITE-OFF —AND A CELEBRATION

Sumitomo's move signals Japan's banks are facing facts

To hear Sumitomo Bank Ltd. board member Masayuki Oku tell it, the latest announcement to rock Japan's beleaguered banking world took shape over the four-day New Year's holiday. While most of the country celebrated, his bank's top managers hunkered down to map out a strategy for the next fiscal year. Their concern: how to deal with \$15.8 billion in bad loans burdening their books since Japan's economic bubble burst in 1990. Says Oku: "They wanted to find a breakthrough."

It seems they did. On Jan. 27, only two months after forecasting a \$600 million operating profit for the fiscal year ending in March, Sumitomo announced it would write down \$8 billion in bad loans and take a \$2.8 billion loss for the same period. The crunching loss is the biggest by a Japanese company in memory and the first by a major Japanese bank since World War II. More important, it is the most open admission yet of bank-loan problems in Japan, where disclosure standards pale by comparison with those in the U.S. and Europe.

Rarely does a monumental loss trigger a celebration. But on the next day of trading, the Nikkei stock index rose by 3.6%, and several top banks' shares—including Sumitomo's—soared by more than 15%. Investors and ana-

lysts alike hail Sumitomo's move as a sign that Japan's banks are starting to climb out of the bad-loan morass that has gripped them since 1990. Japan's leading banks hold an estimated \$133 billion in nonperforming loans (table)—a third of the perhaps \$400 billion in bad loans burdening Japan's financial system. Now, observers believe, Sumitomo's decision could hasten a much-needed restructuring. Says Yoshinobu Yamada, an analyst at CS First Boston (Japan) Ltd. in Tokyo: "This is very good news for the financial industry."

Other major banks may follow Sumitomo's footsteps. Its decision "shows

that banks can deal with their problems by themselves and that there's no need for public funds to support them," Yamada notes. Likewise, Alicia Ogawa, an analyst at Salomon Brothers Asia Ltd., believes that pressure for an industry restructuring may now mount. While she thinks few major banks are strong enough to absorb big write-offs this year, she names Bank of Tokyo-Mitsubishi Bank, Industrial Bank of Japan, Sanwa Bank, and Fuji Bank among those that probably can.

FILTER DOWN. So far, no other major banks have announced write-offs. They may hesitate to imitate Sumitomo because Japanese mores could impel a bank chairman to resign after reporting a loss. Sumitomo finessed this issue because its former chairman resigned in 1993 to take responsibility for loans to scandal-fraught trader Itoman Corp., a major source of the bank's bad debt.

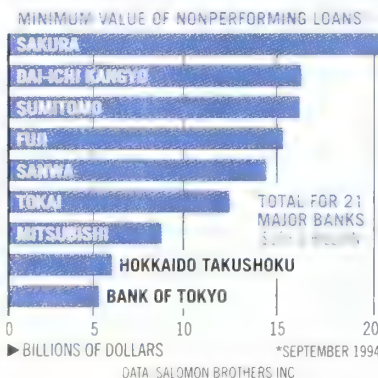
Nevertheless, Sumitomo's move suggests that the regulators now feel comfortable enough with banks' reserves and profitability—and with Japan's recovery—to let the bad news filter down to the bottom line. Until now, bureaucrats at the Ministry of Finance and the Bank of Japan forbade major banks to report losses for fear of undercutting confidence in the financial system. To cover losses, banks sold off pools of equity as the fiscal yearend approached.

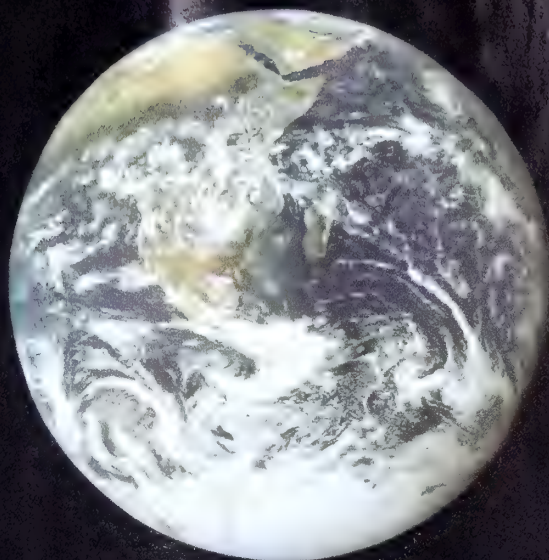
Bureaucrats deny they sanctioned the reporting of a loss. "We don't have the power to stop them from reporting what they want," says Toshio Muraki, a director of the Ministry of Finance Banking Bureau. But Sumitomo's Oku says that for the past year, retired "old boys" from the Ministry and the Bank of Japan have been calling for banks to start taking losses. This was a classic ploy for the agencies to signal their wishes. Oku says Sumitomo's decision was helped along by the recent "confirmation" of Japan's economic recovery, which should spark new demand for loans, and by the bank's cost-cutting, which freed up funds to cover losses.

So, for Japan, Sumitomo's start is important. If other banks now pick up the signal, it could pave the way for more aggressive lending to creditworthy customers, which could boost profits and further aid Japan's recovery. "This will be the year in which dramatic strategies are unveiled to solve the financial system's problems," predicts CS First Boston's Yamada. If so, Sumitomo Bank richly deserves kudos for getting the ball rolling.

By Robert Neff in Tokyo, with William Glasgall in New York

THE BURDEN ON JAPAN'S BANKS





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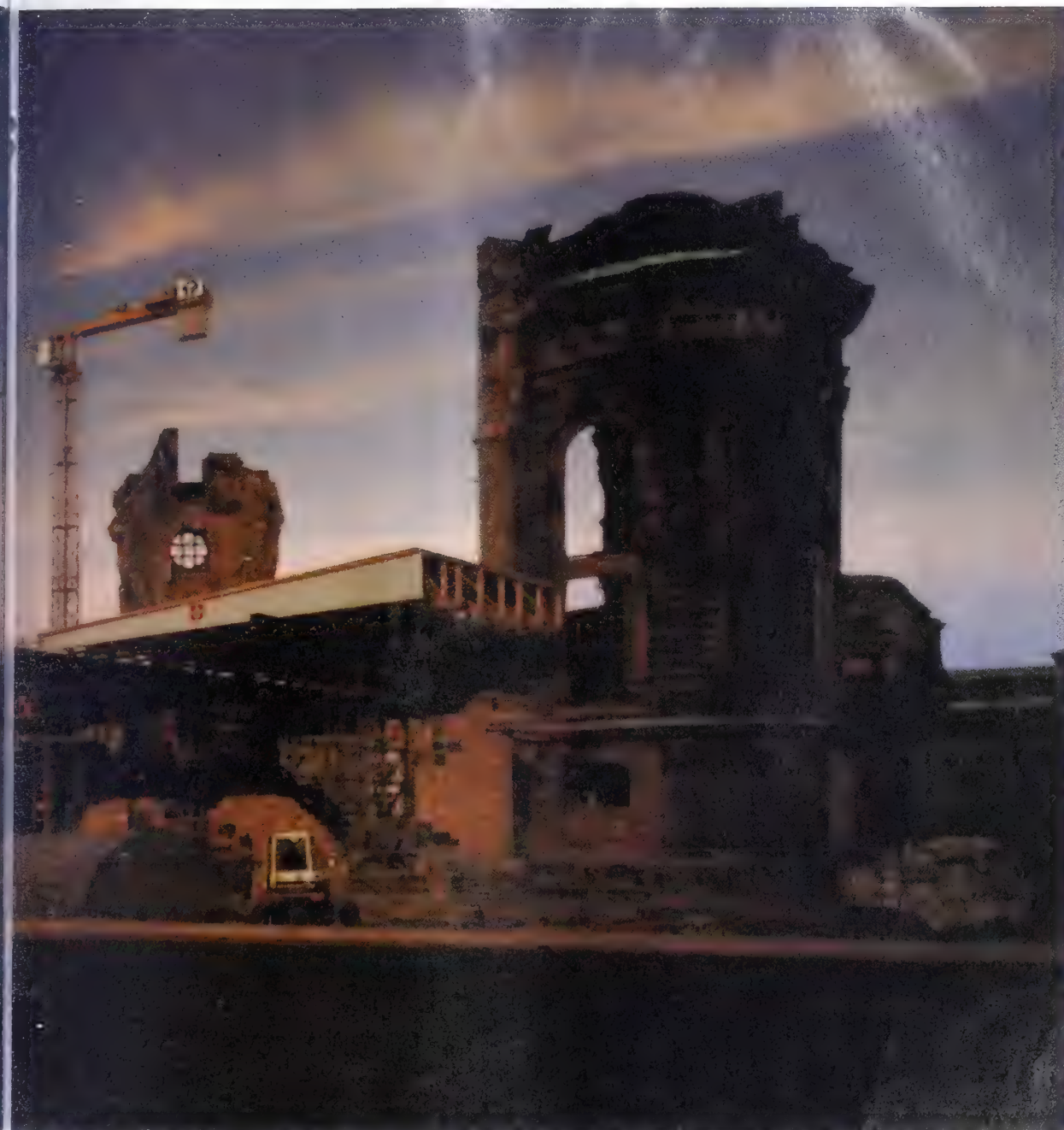
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HONG KONG

EVEN IN HONG KONG, WHAT GOES UP...

The priciest real estate in the world finally slumps

Some of Hong Kong's biggest property moguls crowded into Kowloon's Cultural Center on Jan. 25 to attend the first government land auction of the year. Only one problem—they didn't show much interest in buying land. Of three sites offered, one was withdrawn after attracting no bids, another went to a small-time player who was the sole bidder, and the third sold for just \$22 million, well below the \$25 million the government hoped for.

Only a year ago, Hong Kong was the world's hottest real estate market. Today, it has lost its luster. Rising U.S. interest rates, a falling stock market at home, and uncertainty in China have conspired to hit the colony's residential and commercial sectors. Tumbling prices and rents are a rude shock to property tycoons used to booms, and no relief is in sight.

The residential market is hardest hit. Sales prices have dropped nearly a third from the highs set last spring. Luxury apartments in the Mid-Levels section of Hong Kong Island go for \$1,400 per square foot, down 8% from last year. Commercial rents are also suffering, falling some 10% in the Central District since November.

MISSING CASH. Hong Kong's ailing property markets are also undermining its slumping stock market. Developers make up 30% of the Hang Seng index. Another 30% is composed of conglomerates with major real estate holdings. Banks with big mortgage portfolios make up much of the rest.

The bear market is hurting some of Hong Kong's biggest names. In early January, Li Ka-shing's Cheung Kong Holdings Ltd. put 128 units of its new Laguna City development on the market.

The company had been predicting the sale would be oversubscribed by 400%. But it received only 100 applications—even though the offering prices were 9% lower than similar apartments offered last September. While the volatility is mostly in the residential sector, analysts expect the commercial sector to follow suit. Crédit Lyonnais analyst Trevor Cheung predicts a fall of up to 30%.

And a new factor is unsettling mar-

The picture won't get much better for the land companies in the next few years thanks to a glut of new commercial buildings. In 1996 alone, some 5 million square feet of new grade-A office space will come on the market. So much new space is coming online that many tenants are taking short leases. That means paying rents of as much as \$156 a square foot per year—compared with \$33.60 in Manhattan and \$54 in Singapore—but so tenants will be able to move when prices fall. NBC Asia, which plans to start broadcasting in April, took a two-year lease earlier this winter. "Our hope is that there'll be further slippage in commercial rents by 1996," says Leonard Pratt, NBC Asia's director of network development.

Hard times for property moguls are not that unwelcome to some in Hong Kong. Governor Chris Patten's govern-



A SHOE YET TO DROP

Lots of prime commercial space will soon be coming online

ment, worried about Hong Kong's competitiveness, took steps last spring to push prices down, such as banning the resale of residential units still under construction—virtually ending a rash of speculative buying. The measure will stay in place for while, since the government would like home prices to fall 10% more.

The news is not a bleak for Hong Kong land companies. The decline in prices may lure back foreigners scared off by the colony's reputation as the world's most expensive market. "We still believe there is more demand than supply in both residential and commercial property," says Lily Ye, senior property manager

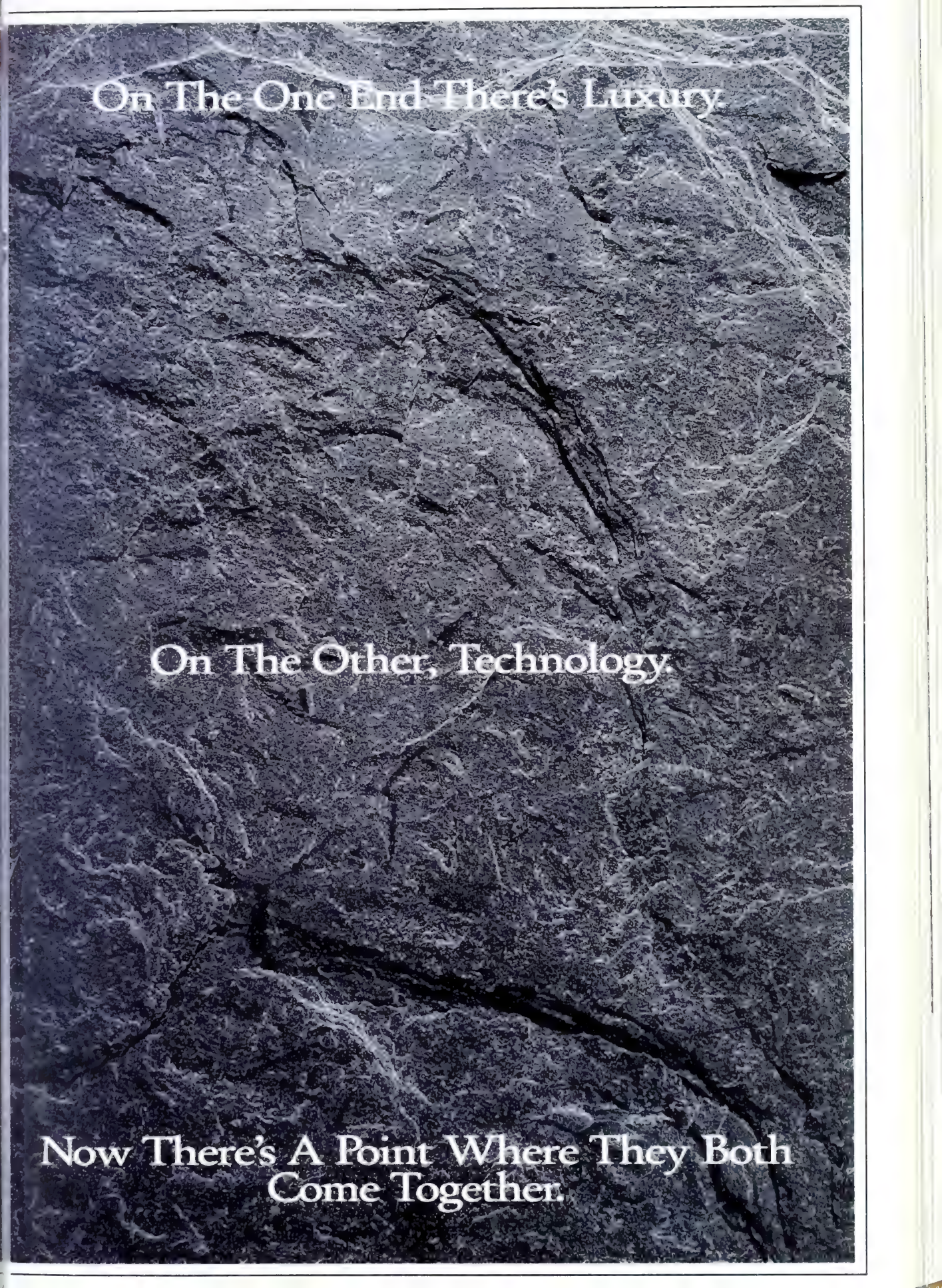
at Midland Realty International, one of Hong Kong's largest realtors.

Even so, the slump has created a new attitude. The punters who reveled in flipping properties have not only suffered monetary losses, says Crédit Lyonnais Cheung. "For years, there was a mindset that you can't lose betting on Hong Kong." To their dismay, the colony's property speculators have learned that they can't win all the time.

By Dave Lindorff in Hong Kong

...does the Hang Seng index

kets: political jitters. Until recently, the property markets had largely ignored the battle of words between London and Beijing over the 1997 succession. But with less than 30 months to go before Beijing takes over, there's more concern about China—especially with Deng Xiaoping reportedly on his deathbed. Moreover, Chinese investment in Hong Kong has dropped sharply, because state enterprises hovering near bankruptcy have much less cash for speculation.



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 **LINCOLN**
What A Luxury Car Should Be

EDITED BY STANLEY REED

ISRAEL: WILL STARING INTO THE ABYSS GET PEACE BACK ON TRACK?

Yitzhak Rabin, Israel's 72-year-old Prime Minister, is certainly no stranger to combat. He has been a central figure in many of Israel's wars, starting with the War of Independence in 1948. But rarely has he been so embattled as now. Agreements painstakingly worked out in Oslo and Cairo with the Palestine Liberation Organization's Yasser Arafat are in tatters. Terrorist attacks against Israelis since Rabin and Arafat shook hands in Washington 16 months ago have killed 48 Israelis dead. And recent polls show that only 28% of Israelis support Rabin, compared with 50% who back Benjamin Netanyahu, his telegenic archrival in the conservative Likud Party.

It is as elsewhere in the Middle East, where peace arrangements may be deceptive—and Rabin's peace process may have a lot of enemies yet. Israeli, Egyptian, Palestinian, and Jordanian leaders are trying to get things back on track with a Feb. 2 summit in Cairo. "Sometimes things don't work out until people stare at the possibility of failure and take it seriously," says Ambassador B. Quandt, a Middle East specialist at the University of Virginia.

Interest is focusing on the idea of separating Israel from the Palestinian areas of the West Bank and Gaza. The point is to protect Israelis, but separation would also speed up creation of a de facto Palestinian mini-state, and, therefore, also appeals to the Palestinians. A peace between two carefully separated states, many Israelis and Palestinians are starting to realize, will probably be easier to maintain than the borderless common market promoted until recently. "Theoretically, separation should be good for the Palestinians," says Gil Feiler, Managing Director of Info-Prod, a Washington-based economic consulting firm. "It could lead to improved cooperation in the long run."

In late January, the Israeli Finance and Police Ministries moved to set up emergency working committees to

plot the mechanics of separation. Meanwhile, Jerusalem is moving quickly to make up for the loss of the Palestinians who had done a lot of the low-paid work in the Israeli economy by speeding up entry procedures for workers from Thailand and other countries. For the first time, there are more foreign workers in Israel—45,000—than Palestinians.

Despite its anemic showing in opinion polls, Rabin's government is in little danger of losing majority control of the Knesset until scheduled elections in summer, 1996. Then the big question mark will be the potent new swing vote represented by Israel's 500,000 recent Russian immigrants. But Russian voters are more disenchanted over the difficulty of finding well-paid jobs than anxious about security.

CRACKDOWN. In the meantime, Rabin is also getting some badly needed reinforcement from the Clinton Administration, which took a backseat to Israeli and PLO negotiators in recent months. With a visit by Secretary of State Warren M. Christopher to the Middle East expected in a few weeks, Washington's role as power broker is intensifying. One subject for Christopher's agenda: speeding up the \$500 million



FENCING OFF: Separate by choice?

U.S. aid to Palestinians as an incentive for Arafat to crack down on extremist groups such as Hamas and Islamic Jihad.

In the end, that aid could prove crucial. The danger of Rabin's gamble on separation is that closing the borders strangles Palestinian areas economically—thus playing directly into the hands of Hamas and other groups. And Israelis also worry that even cordoning off Palestinian areas might not stop terrorist acts. Israeli settlers in the West Bank would still be vulnerable, and Israeli police report that Palestinian groups can now forge Israeli identity cards. The bottom line is that the peace process is continuing, but the peace could wind up looking very different than expected.

By John Rossant in Rome and Neal Sandler in Jerusalem

GLOBAL WRAPUP

OTHER BLOW FOR HUNGARY

The crisis of confidence in Hungary is worsening. Finance Minister László Bokros has resigned, depriving former Communist Premier Gyula Horn of his most respected economic official. Bokros was responding to Horn's taking the privatization portfolio away from his ministry. Horn has also fired privatization chief, Ferenc Bartha. The Prime Minister recently criticized Bokros to raise \$1.5 billion through sales of stakes in the state-owned oil, gas, and electric companies.

With privatization in trouble, analysts are focusing on Hungary's rising current account deficit and its substantial external debt, equal to two-thirds of gross domestic product. A devaluation of the forint, whose value the government controls, is expected.

CHINA BREAKUP?

► A study ordered by the Defense Dept. on China's future after Deng Xiaoping concludes that the most likely scenario is a breakup of the Middle Kingdom within seven years of Deng's death. The consensus of the

panel of outside experts who wrote the report, *China in the Near Term*, was that there was a 50% chance of a "Soviet-style breakup."

Surprisingly, the study panel's chairman, Ronald A. Morse, director of international programs at the University of Maryland, argues that such an outcome could be preferable to the status quo. Disintegration into a loose federation of economically driven regions would lessen China's military threat to its neighbors and reduce its obsession with sovereignty, he thinks.

TRADERS

A WINDY CITY SQUABBLE THAT'S REALLY THE PITS

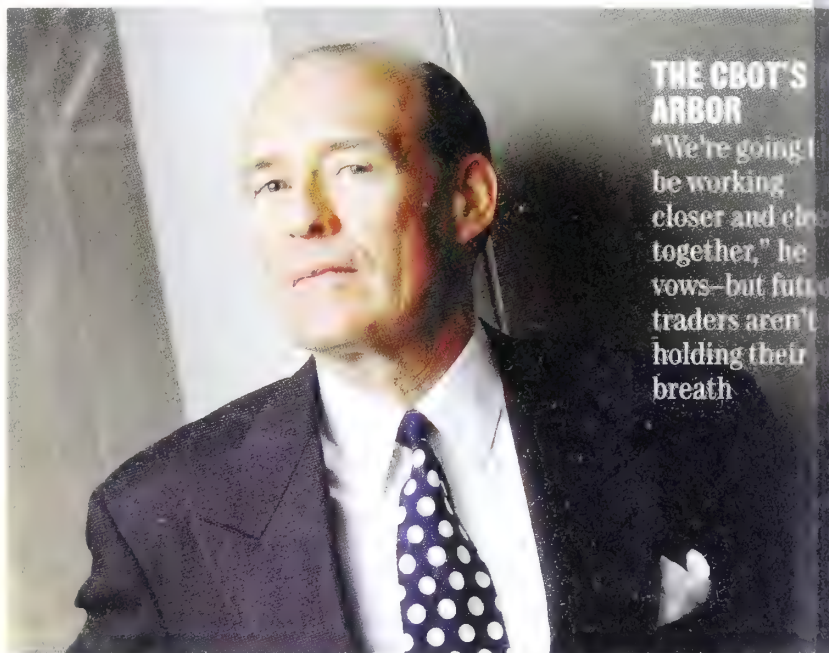
The feud between chairmen is hurting Chicago's exchanges at the worst possible time

At first glance, Pat Arbor and Jack Sandner seem like they were made for each other. Both overcame troubled childhoods on Chicago's streets to hit it big in the Windy City's famed commodity pits. Both rose to become chairmen of their respective exchanges—Arbor at the Board of Trade and Sandner at the Mercantile Exchange. Patrick H. Arbor, 58, is a doting grandfather. John F. Sandner, 53, shares his home with seven adopted children. Both are health nuts: Arbor climbs world-class mountains, and Sandner, a one-time boxer, works out routinely in the gym adjoining his office.

So why can't these guys get along? In the two years since Arbor assumed the helm at the Board of Trade, the Chicago exchanges have become a battleground. Instead of working together to make their institutions more efficient and customer-friendly, an ugly personality clash has Sandner and Arbor operating at cross-purposes. Meanwhile, innovative foreign exchanges such as London's LIFFE, Paris' MATIF, and Brazil's BM&F have developed attractive new contracts that are stealing an increasing share of worldwide futures-and-options trading. While Arbor and Sandner have fiddled, Chicago's status as the global center of futures trading has eroded (charts).

KEY TECHNOLOGY. There isn't much the two won't fight about. Disputes have ranged from petty squabbles, such as which exchange has more volume, to destructive bickering over critical issues. Last year, for instance, bitter infighting split a proposed partnership for the Globex electronic-trading system, a key link to customers overseas. Arbor's Board of Trade went off in a huff to develop its own system, and now futures traders have to learn both. Fighting also scuttled efforts to unify trade-clearing and banking, moves that would have sliced administrative costs at both exchanges while bettering their ability to guarantee trades.

Many fear that if such behavior contin-



THE CBOT'S ARBOR

"We're going to be working closer and closer together," he vows—but futures traders aren't holding their breath

ues, the next casualty will be a current joint effort to develop handheld trading computers, a key technology aimed at reducing costs and curbing fraud in Chicago's turbulent markets. "It's just nuts for the two exchanges to be fighting each other when the real competition is overseas and in over-the-counter markets," says John F. Benjamin, managing director of Smith Barney Inc.

Even in a world where paramedics stand by to treat injuries from the daily ruckus in the pits, Sandner and Arbor "appeared stupid and silly," says Robert K. Wilmouth, who heads the National Futures Assn. "They probably recognized that." Indeed, in recent months the two chairmen insist that they have cooled down their feud. Sandner attributes their disagreements to a "learning curve" as the pair got to know each

other. "That's now out of the way," says. "We can take the confrontation out of the issues." Arbor concurs: "We're going to be working closer and closer together."

But futures-industry members are holding their breath. "The nature of the business is competition," says John Damgard, president of the Futures Industry Assn. "It makes it almost

JOINT EFFORTS HAVE SOURED

SCUTTLED A joint venture for Globex, a computer work that allows 24-hour trading for customers worldwide. The Board of Trade has launched a computer system, increasing costs for customers that use

SUNK Negotiations for unified trade-clearing and banking. Common clearing would streamline and cut costs for both customers and the exchanges

THREATENED Development of handheld trading computers. Billed as an antifraud measure to replace paper cards still used to record transactions, the devices also would reduce errors and cut clerical

ible for them to shake hands and "We are Chicago." To a degree, the trouble between Arbor and Sandner reflects a longtime rivalry between their constituents—the nervous, sweaty floor traders who viewed one another as the competition for generations. But it's more than that. For all they seemingly have in common, the two chairmen also have differing personalities. Sandner, the for-boxer, is combative and decisive. Arbor, the cerebral mountain climber, is a charmer who relies on smooth talk and compromise to win his way. What they share is a fierce stubbornness. All it takes is a volatile brew.

contest victory that landed him on the front page of the *Chicago Sun-Times*. Arbor hit bottom as a teen when his divorced mother's drinking forced him into Mercy Home for Boys & Girls, a Catholic-run orphanage in Chicago.

Strangers helped them both. For Sandner, it was former world middleweight champ Tony Zale, who saw potential in the unruly teenager and persuaded Sandner to clean up his act. Under Zale's iron thumb, Sandner became a disciplined amateur boxer with a 58-2 record. He made up lost time at a new high school and won an athletic scholarship to the University of Arizona.

Likewise, Arbor found role models

erns. As a teetotaler, he pushed for reforms but also answered a want ad for a Board of Trade grain company. Within a few years, he hit it big as a trader—then went bust. He rebuilt his stake by working in construction and returned to the pits for good.

SHOUTING MATCH. Both men became well-regarded futures executives and worked hard in exchange politics. Sandner took over the Merc in 1991, Arbor the Board of Trade two years later. Before then, the exchanges were pushing for cooperation. And though the chairmen vowed to continue and arranged a few one-on-one dinners to discuss the future, the honeymoon didn't last.

One by one, common ventures fell apart. A plan to unify trade-clearing operations exploded in mid-1993, when Sandner formed a separate partnership with the New York Mercantile Exchange. In dueling press releases, an angry Arbor accused Sandner of bad faith, while Sandner claimed to be "surprised and disappointed" by Arbor's reaction. The acrimony spread into Globex negotiations, with Arbor accusing Sandner of going behind his back to hold private meetings with their fellow partners. Sandner denies this. By last year, the feud spilled into Chicago Mayor Richard M. Daley's office. Hizzoner had to separate the pair during a shouting match over how to organize a charity boxing benefit pitting Board of Trade members against Merc members.

While both insist such antics are behind them, insiders fear the development of handheld trading computers will be the next initiative to sour. Not surprisingly, the two have different strategies for pushing ahead with the system—how fast to introduce it and how much to spend on future development.

Even if the handheld-computer project proceeds, there are other problems. Given the foreign competition, Arbor and Sandner will need to work as teammates to keep from slipping further behind. Most of Chicago's volume growth has come from contracts introduced more than a decade ago. And a blockbuster product of the future is nowhere in sight. Member firms say that instead of bickering over mutually beneficial issues such as unified trade-clearing, the exchanges should be looking hard for that new competitive weapon.

In fact, many members think Arbor and Sandner should merge the exchanges to provide a unified front against competition. Both chairmen say they'd consider it. But in the elbow-throwing, every-man-for-himself atmosphere of Chicago's pits, unity is already an elusive concept. And Sandner and Arbor have enough trouble just being civil.

By Greg Burns in Chicago



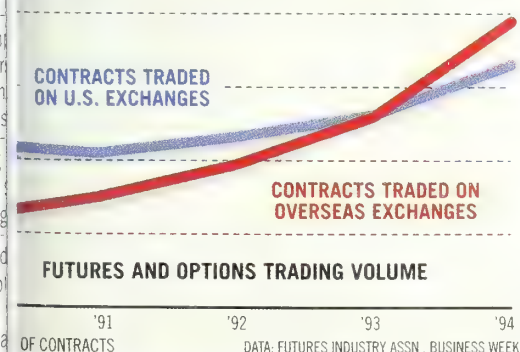
MERC'S SANDNER
Background similar to Arbor's hasn't prevented spats over issues large and small in a shouting match in Mayor Daley's office

though they grew up in different neighborhoods, Arbor and Sandner both were born into troubled working-class, Italian families. Each suffered because of a parent's alcoholism. Sandner, who had a hard-drinking father, dropped out of Catholic high school at age 16 to get a job. It didn't help that his straight-laced teachers disapproved of his one accomplishment: a citywide dance-

in the tough priests at Mercy Home. A bookish kid, he embraced their stoic philosophy. To this day, he has never sampled alcohol, tobacco, or caffeine. He trains to the point of exhaustion for his climbing expeditions. "They're fiercely independent people who've had to fight hard for everything they've gotten," says Hal T. Hansen, president of Cargill Investor Services Inc.

Neither had auspicious starts in the pits. Sandner, who attended University of Notre Dame Law School, started practicing law in Chicago but traded pork bellies during his lunch hour. He lost his first stake within a few weeks but soon got the hang of it and gave up law for live-stock futures. Arbor started out teaching high school and then served as mayor of Harwood Heights, a blue-collar Chicago suburb known for its all-night tav-

FOREIGN RIVALS ARE BENEFITING





Cover Story

GO-GO GOLIATHS

These giants keep on expanding—just like scrappy startups

The People Dept. at Southwest Airlines Co. is bracing for a long, grueling Saturday. But unlike some other companies' personnel sections that have to put in extra hours, it's not preparing mass layoffs. Instead, staffers will be interviewing 200 internal candidates applying for the 100 management jobs opening up in reservations—thanks to Southwest's rapid expansion.

Over at Home Depot Inc., it looks as if the retailer didn't come in exactly on target for store openings last year: The old goal was a 25% increase, to 330 stores. Instead, the chain finds itself with 340 locations, a 29% jump—after investing \$150 million in a joint venture in Canada (page 65).

And in an era of belt-tightening, Microsoft Corp. worries that its staff is getting too accustomed to riches and success. In a memo last year, the company chided managers all over the world for catered lunches and little gifts for good work. It complained that things had gotten so far out of hand it wouldn't be surprising to see handouts of leather Gucci jackets with the Microsoft logo.

Oh, to have problems like these. As other corporate giants continue to downsize, rightsize, and reengineer their way of doing business, supposed health, highfliers such as Microsoft, Home Depot, and Hewlett-Packard are proving that big doesn't necessarily mean bumbling. And they're not alone. Thundering through industries as diverse as retailing and steelmaking are scores

Home Depot

Liam Harris, senior vice-president, corporate development

Liam E. Harris takes seriously Home Depot Inc.'s mantra about being close to the market. For years, as the retailer's senior vice-president for corporate development and its real estate executive, visited a plot of land the company wanted. And with Home Depot planning to increase its outlets by 25% a year that meant quite a bit of racing. But by 1998, the Atlanta-based company aims to have opened a total of 1,000 stores, including 460 new ones—in Canada, Mexico, and the United States—so Harris, 60, has decided to stick with tradition and skip a few shortcuts. "I physically can't do it any more," he says. Physically, perhaps not. But electrically and telephonically, Harris stays on top in executing Home

Depot's expansion of its home-improvement and garden-supply network. The chain faces the same problems as an army in a war of conquest: seizing the right territory, maintaining supply lines, controlling occupied terrain, and planning offensives.

Home Depot assaults new fronts in distinct waves. The first wave, Harris says, "plants the flag"—putting three or four stores on the perimeter of a designated city. Each store typically serves 100,000 households, which have median incomes of \$45,000. And 75% of those households are owner-occupied. Once the initial stores reach combined sales of about \$50 million, Harris' second wave fills in the territory with new outlets designed to make Home Depot dominant over three to five years.

The campaign doesn't stop there.

When sales surpass Home Depot's average of \$400 per square foot, or when growth lags behind the inflation rate, Harris figures that a store is getting too crowded: Home Depot will close a thriving store and open two smaller ones to improve the shopping experience for customers, a tactic Harris calls "cannibalizing."

As long as demand for its wares keeps growing, Harris doesn't worry about overbuilding. Instead, he used to fret that he wouldn't find enough real estate veterans to manage Home Depot's growth, but the property debacle of recent years has glutted

the employment market with realty pros. "We're finding lots of people with trench warfare experience," he says. And Home Depot is making sure they're armed with the customer data they need to map a winning campaign.

By David Greising in Atlanta

OPENING UP

Home Depot wants to increase the number of its stores by **25%** a year

able Go-Go Goliaths. For years, these companies have thrived in the kind of swift, sure growth more often found in fleet-footed entrepreneurs. They're grabbing new markets, churning out better products—and coping with rising costs and ballooning bureaucracies. In all, BUSINESS WEEK has identified 10 companies that demonstrated these talents while achieving growth in sales and profits that put them well ahead of the herd. This admittedly subjective list isn't all-inclusive: There are other big corporations that fit the bill. But these companies are the clear standouts, and they represent a wide variety of industries and competitive situations.

KNEE-JERK NAYSAYING. Absent from the list are such illustrious companies as General Electric, AT&T, Johnson & Johnson, and others. That's something of a surprise, because steady performers at some of these companies—and sharp turnarounds at others—have given the lie to some knee-jerk naysaying about big corporations in recent years. For one, has reinvented itself—from the shop floor to the executive suite. Along the way, it has sped up introduction of models such as its popular compact Neon. Likewise, AT&T, downsizing, is chasing new success with all the vigor of a startup. Its acquisition of McCaw Cellular Communications Inc. propelled T&T into a leading position in wireless communication.

There are also a few large companies that have grown richly despite changing environments. Johnson & Johnson,

for example, has thrived in the roiling health-care industry, thanks to a decentralized management that allows various units to operate almost as independent companies.

And of course there's GE, which has evolved into the very model of a thriving behemoth under John F. Welch Jr.'s relentless, hard-driving management. GE shows that conglomerates don't necessarily grow at a glacial pace. In the five years ended in 1994, GE's sales and profits have grown at average annual rates of nearly 4% and 9%, respectively.

Such growth is nothing to sneeze at for a \$60 billion company. Still, even these giants don't match the phenomenal records of the Go-Go Goliaths. These exemplars turn in sales and earnings growth well into double-digits, far outstripping their big-company brethren. And in the era of the pink slip,

The Go-Go Goliaths And Their Sizzling Returns

COMPANY	'94 SALES MILLIONS OF DOLLARS	'94 PROFITS	AVERAGE ANNUAL CHANGE*			
			SALES	PROFITS	STAFF	MARKET VALUE
WAL-MART	\$67,345	\$2,333	28%	23%	18%	16%
HEWLETT-PACKARD	24,991	1,599	16	15	1	22
MOTOROLA	22,245	1,560	18	26	3	40
INTEL	11,521	2,288	30	44	7	39
HOME DEPOT	9,239	457	36	44	31	51
MICROSOFT	4,649	1,146	44	48	32	42
VF**	4,320	246	12	10	8	24
U.S. HEALTHCARE**	2,645	300	29	126	21	67
SOUTHWEST AIRLINES	2,592	179	22	31	18	58
NUCOR **	2,254	124	14	11	3	43
AVERAGE CHANGE % FOR ALL BIG COMPANIES†			7	-0.25	0.67	11

*Growth rate measured over five years, using latest available data **1993 data

†Includes those with annual sales of at least \$2 billion

DATA: STANDARD & POOR'S COMPUSTAT, A DIVISION OF MCGRAW-HILL INC.

many are adding employees at an equally rapid pace.

Diverse as they are, these leviathans offer lessons that are of use to the rest of Corporate America. After a decade of watching IBM, General Motors, and Sears Roebuck brought

low, we've come to think of big companies as plodding and

Cover Story

arthritic: too ponderous—and too imprisoned by their past—to cope with technological upheaval in lightning-fast global markets. But at the very core of these Go-Go Goliaths is a culture that embraces change. Above all, they're willing to abandon long-cherished formulas to adapt to market realities. "Good companies not only can learn. They've also learned to forget," says C. K. Prahalad, professor of business administration at the University of Michigan and co-author of *Competing for the Future*, which offers companies strategic insights into the coming years.

BE NIMBLE. Of course, some of these titans enjoy virtual monopolies of their own creation—Intel, for example. And others, such as Home Depot, have carved out unique market niches. But history is littered with once-pioneering companies that lost out to faster, nimbler rivals.

That's why these giants are often willing to make their products obsolete before rivals do. Consider Hewlett-Packard Co. (page 67). HP's latest ink-jet printer, introduced in October, replaces a black-and-white model launched last March. The old model was the world's best-selling computer printer, but the new one offers color, not just black and white. With the optional color-printing kit, the new model costs \$414—just \$49 more than the monochrome one. "We've developed a philosophy of killing off our own products with new technology," says Lewis E. Platt, HP's chief executive. "Better that we do it than somebody else."

Just as important, these giants have managed to stay fresh and forward-looking. By their nature, small companies are flexible and customer-focused. But big outfits need mechanisms and management tools to institutionalize those qualities. That's why many successful giants pride themselves on lean management. Even though Nucor Corp.'s annual sales top \$2 billion, the steelmaker's one-story headquarters in a suburban Charlotte (N.C.) office park is staffed by only 23 people. There are no lawyers and no public-relations officers. And when guests come, Chairman F. Kenneth Iverson escorts them to what he jokingly describes as the "corporate dining room"—a lunch counter across the street.

The payoff for acting small while thinking big comes in the kind of returns usually seen at small hot-growth companies. As other retailers suffered through a consumer drought in



recent years, revenues at Home Depot climbed by 30% a year in the five years ended in 1994, while profits grew a year. Microsoft's five-year record is also stellar: Sales and profits at the software colossus have increased by more than 47% and 53% a year, respectively. The contrast with the mill big companies is stark: Since 1989, average annual sales—for companies in the \$2 billion-plus league—has grown by a modest 7%, while net earnings dropped steadily every year, according to Standard & Poor's Compustat.

The payoff extends all the way to Wall Street. In a recent study of the largest U.S. companies, Mercer Management Consulting Inc. found that investors will pay at least 10% more for an added dollar of profit generated through revenue growth than for that same dollar produced by cost reductions. In retail, for instance, Mercer found that Home Depot's compound annual growth in market value from 1989 to 1994 was 58%, compared with only 12% for profitable cost-cut-

Lessons From The Thriving Giants

What are they doing right?

Diverse as these leviathans are, they have something to teach the rest of Corporate America

ACCEPT CHANGE The marketplace is in constant flux. That means goals and procedures must be continually reviewed and updated. Strive to make your own products and services obsolete: If you don't, rivals will.

LISTEN TO CUSTOMERS They're the best gauge of how a company is faring against competitors. Involving them in the process of developing new products and services helps guard against isolation and arrogance.

DECENTRALIZE AUTHORITY Decentralized decision-making is key in fighting creeping bureaucracy. Quick decision-making is also essential for competitiveness. Lower-level managers who are close to customers and markets need the say-so to make

HIRE CAREFULLY Sign up salespeople at all levels who demonstrate versatility and responsiveness. Growth often strains any organization's ability to maintain its staff quality and supervision.

Hewlett-Packard

James Olson, general manager, Video Communications Division

It looked like mission impossible back in May 1992, when Hewlett-Packard General Manager James D. Olson was told to plunge his division—then a maker of microwave test gear—into the hot market for digital video. He had 11 months to get his nerdy engineers to develop a suite of products—such as computers to send movies to homes—and get them to market.

A daunting task? Sure. But at a company that prides itself on its swift response to changing markets and counts on products that are less than two years old to generate more than 60% of its current equipment orders, it certainly isn't uncommon. In 1994 alone, Olson's Video Communications Div. has suddenly made dark horse HP a

leader on the Infobahn. It has signed deals to supply video computers to Pacific Telesis Video Services, BellSouth, Southern New England Telephone, and the

government of Singapore. Time Warner Cable Group's video-on-demand trial in Orlando will include a special HP printer that lets users pluck still images off video.

"We've transformed ourselves from gearheads into gladiators," says Olson, 44, an electrical engineer who joined the company in 1974.

The key to the transformation: a complete revamping of product development. The unit, which used to take up to six years to develop new offerings, now takes less than nine months. How? First, Olson had his engineers consult with potential customers. That way, they knew what

features to include, avoiding endless tinkering. Then, they simplified manufacturing by using common parts. Many products use the same power supplies, for example. They even decided to buy some components and software from outside sources rather than develop such gear more cheaply in-house, as long as that approach speeded development.

For example, HP initially purchased converters that adapt various video formats from Britain's Vistek Electronics Ltd. and sold them under the HP logo. At the time, such deals were almost unheard of. But in the

NEW MARKETS

At Hewlett-Packard,
new products
account for more
than
60%
of its orders

race to come up with new products, the practice has become far more common. These days, pleasing the marketplace takes precedence over tradition.

By Robert D. Hof in
Santa Clara, Calif.

as Ames Department Stores Inc. "You can't shrink to fitness," says Dwight L. Gertz, a Mercer vice-president. That's a notion employees can certainly appreciate. Instead of laying out pink slips, many of these behemoths have ended their payrolls. At Microsoft, with 16,000 employees, payrolls have grown an average of 32% a year since 1989. Contrast, the average payroll of all big companies has ended by less than 1% a year, according to S&P.

Once they're not distracted by restructuring, Goliaths can devote energy to what they do best: responding to opportunity with astonishing agility. In October, Microsoft CEO Bill H. Gates III made an exception to his long-standing tactic of developing his own products: He agreed to pay \$1 billion for Intuit Inc., which produces personal-finance software. Gates hopes for a leg up in the rush to provide financial services on the Information Superhighway.

Similarly, with rivals Continental and United aiming to

replicate Southwest's low-fare, short-haul formula, Southwest has accelerated its expansion. After acquiring Morris Air Corp. in late 1993, Southwest Airlines Co. upped its capacity by 29% in 1994. "When you have this tremendous flux in the outside world, you don't want to get 'fluxed' yourself," says CEO Herbert D. Kelle-

her. True, Southwest recently announced that fourth-quarter earnings fell 47%—largely the result of fare-discounting to defend its niche. But profits are expected to resume growing by at least 12% a year over the next five years, after a projected 7% increase this year, estimates Michael W. Derchin at NatWest Securities Corp.

SHRUNKEN TURF. There's irony, of course, in the discovery that big isn't always bad. After all, for most of Industrial America's history, large outfits have been envied for their cornucopia of advantages: economies of scale, market clout, and vast resources—of capital, facilities, technology, and talent. Those riches have enabled big companies to expand both at home and abroad. But in recent years, as markets fragmented and competition intensified, many giants have spent more time defending their empires than conquering new territory. They became champions of the status quo.

IBM, for example, remained wedded to the mainframe long after the emergence of lucrative personal computers. Sears, in an effort to protect its private-label products, stubbornly refused to stock the brand-name appliances that shoppers demanded. GM and Ford Motor Co. were both slow to capitalize on the growing demand for minivans—out of fear of cannibalizing their conventional station wagons. All too often, such efforts to defend turf have yielded nothing but a smaller turf. The upshot: The chief skill possessed by legions of U.S. managers is the art of shrinkage. But paring costs and slashing jobs are no substitute for growth. "Getting lean and mean is no small thing, but lean and mean is not a business strategy," says management guru Tom Peters.

For fast-growing Goliaths, mass remains an awesome weapon. Consider \$11.5 billion Intel. With its near-monopoly on the most lucrative kinds of microprocessors—the brains of PCs—Intel has more resources than its rivals to lavish on research and development: It will spend more than \$1 billion this year on R&D, compared with \$275 million by Advanced Micro Devices Inc., its nearest competitor. Neither the dis-

I CONTINUOUSLY Don't
on training—even in lean
improving employees' skills is
to a company's ability to iden-
sh opportunities and respond
changing markets.

ROL COSTS Financial targets
ful. But it's just as important
a frugal corporate culture
the example of top manage-
lavish perks send the wrong
e to employees.

covery of a bug in its new Pentium chip—nor the slowness that it showed in responding to customer concerns—is apt to erode its commanding lead, according to analysts. Sheer size is also an advantage for Microsoft. But because of its near-

Cover Story

aggressive sales tactics, competitors have captured the attention of federal regulators with allegations of unfair practices. Microsoft denies any wrongdoing.

The challenge is to make sure bigness doesn't lead to bloat. These Goliaths preached frugality long before it became fashionable. Microsoft follows what it calls the "n-minus-one" theory of head-count growth: If five extra people are needed for a task, Microsoft will allocate four. Surprise! The work gets done anyway. At Southwest, capital expenditures of more than \$1,000 must be approved by a department head, the chief operating officer, and the vice-president for finance.

FORGET MEMORANDUMS. Watching pennies, however, is only one aspect of bureaucracy-busting. Some big companies exhibit a cultural antipathy to perks and red tape. Like all top Intel managers, CEO Andrew S. Grove has a cubicle, not a private office. And when they travel, executives fly coach and rent subcompact cars: Ford Escorts are jokingly known as "Intel limousines." Meanwhile, at U.S. Healthcare Inc., one of the nation's biggest and fastest-growing health-maintenance organizations, meetings are prohibited between 9 a.m. and 4 p.m., and memos are banned.

Others have reinvented their management structures to combat the almost inexorable urge to centralize. "It's something you have to work at all the time," warns Hewlett-Packard's Platt. In the 1980s, HP almost collapsed under the weight of 38 central committees that ruled on everything

monopoly in personal computer operating systems and its highly

from product pricing to where a new product should be launched. In 1990, Platt's predecessor, then-CEO J. Young, dissolved the committees and decentralized almost every aspect of HP's business. Instead of relying solely on a central R&D staff, as many companies do, HP hands over most of its massive \$2 billion research budget to its four operating groups to spend as they wish. "You can't spend \$2 billion efficiently in any kind of centralized way," says Platt.

Lean and responsive management alone won't hold rivals at bay, of course. Thriving Goliaths also never lose sight of the marketplace. Motorola Inc., for example, encourages wireless divisions to compete against each other—on the theory that the marketplace will ultimately pick the winning technology. The company's General Systems Sector, which is developing a new technology to increase the calling capacity of cellular networks, is going head-to-head against Land Mobile Sector, which has joined with Nextel Communications Inc. The two are developing a multi-use wireless service that will offer everything from calling to text paging.

Close contact with customers also means more business. For instance, VF Corp., maker of Lee and Wrangler jeans, has linked its computers to those of its retailers. Now, it tracks daily sales and replenish stocks automatically, with cumbersome order forms. That makes for happy customers—and bigger orders.

Microsoft goes even further when it comes to customer contact. In December, it delayed the release of its Windows operating system until August—partly the result of an unprecedented level of testing. Although analysts reckon the delay could slow Microsoft's revenue growth to 5% this quarter and next and cost it millions in potential earnings this year, most are betting Windows 95 will revolutionize software applications and eventually generate a windfall for the company.

The testing began in 1992, almost immediately after the introduction of Windows 3.1. Engineers sat down with fo-



ps made up of users from a couple of a companies to find out what new features and capabilities they wanted. From they came up with the Ten Commandments for Windows 95, including more user-friendly graphics. Then came usability studies in 1993. In a lab at headquarters, Microsoft asked experienced and inexperienced users to try the new features. Reviewers behind one-way mirrors noted easy or tough a time people had. Last year, Microsoft started field studies. A "beta" version was sent to 40,000 customers, to provide independent feedback.

Microsoft kept attuned to customers, successful products have pushed decision-making down to the managers, who know the market first. Each of Nucor's 21 plant managers is responsible for sales, purchasing, and personnel. Sure, it might be cheaper to centralize those functions at headquarters. But the steelmaker

values the cost of duplication is more than outweighed by improved responsiveness to the marketplace (page 70).

APPLICANT IN 10. Naturally, if they want lower-level managers to take on more responsibility, companies must ensure they have the needed skills. That's tough when a company is moving at a breakneck pace. At Motorola, which has 13,000 employees in 1993, every job candidate, even those looking for factory work, goes through three days of interviews. During that time, applicants write a composition and take 4½-hour tests—in math, problem-solving, and ability to work on a team. Only one candidate in 10 makes the cut. At Southwest, the hiring process is called "targeted selection." For instance, the airline interviewed 35 of its best applicants to find what qualities they had in common. One key

There's no guarantee the Go-Go Goliaths of today won't stumble later on: It took IBM more than 70 years to flounder

trait it discovered was a willingness to work as part of a team. (After all, it's not unusual for Southwest pilots to help flight attendants tidy cabins after a landing to speed airport turnarounds.) Southwest now uses those characteristics to evaluate applicants (box). Last year, Southwest's turnover was about 7%, including retirements—half the industry average.

Staff training is also critical if big companies are to maintain their standards and corporate culture in the face of constant expansion. Once in the door, the typical Motorola employee gets 40 hours of training a year to refine such skills as teamwork and problem-solving. Employees can also take courses at their factories in communications and technical skills or can attend classes at Motorola University at headquarters in Schaumburg, Ill. Motorola spends about 4%

of its payroll cost on training and development, compared with an average of 1.2% for all U.S. companies. Thanks to its motivated workforce, Motorola says the quality of work at its manufacturing sites has steadily improved. The company calculates it has scarcely 30 defects for every 1 million opportunities there are to make mistakes, down from 7,000 defects in 1987.

The healthy giants also make exhaustive efforts to motivate and communicate with employees. For example, Kelleher and about 90 of Southwest's other top executives spend at least one day a quarter in the field, working in areas outside their own departments. Of course, pay is an important motivator, too. At successful Goliaths, pay for performance isn't a concept limited to the executive suite. Steelworkers at Nucor, for instance, are eligible for productivity and quality bonuses that are typically 130% to 150% of base pay. That can

Southwest

Rita Bailey, manager, corporate employment

Four women are chatting amiably about everything from their hoods to tough problems they've faced on the job. But what might seem like nothing more than a friendly kaffeeklatsch is actually an informal job interview at Southwest Airlines Co. The four are competing for openings in the airline's "special marketing" department, which aims to attract as passengers more businesswomen, elderly travelers, and young people.

Leading the session is Rita V. Bailey, the energetic manager of corporate employment. Dressed in blue jeans, a red polo shirt, and a cardi- Bailey, 42, has managed to turn a potentially tense situation into two hours of relaxed conversation. It's what Southwest takes job interviews lightly. But the airline finds

that an informal approach yields more information than stiff, one-on-one meetings.

While other companies might consider human resources a backwater, the People Dept. at Southwest "is like the keeper of the flame," says Treasurer John D. Owen. Lately, the 125-member department has been taxed to its limits. Over the past four years, Southwest's staff has increased by 97%, to about 17,000 employees. Despite Southwest's breakneck growth, Bailey insists that the company won't compromise quality to speed up its hiring process. For this marketing opening, Bailey has already interviewed 22 applicants, including the four women above. And she's likely to call in an additional half-dozen for consideration.

In this case, the marketing background of the four applicants is important. But Bailey, who joined the airline 17 years ago as a ticket

agent in El Paso, and Camille T. Keith, vice-president for special marketing, seem more intent on finding a self-starter who has a willingness to pitch in on any job, even blowing up balloons for festive events. One candidate says that she has always wanted to be an entrepreneur and boasts of her accomplishments in her current job, often using the word "I." Bailey and Keith worry she'll

need too much stroking and won't fare well on a team.

The Southwest managers also study subtler clues—how the candidates interact. "We just want the kind of person who can relate to everybody and everything,"

says Bailey. In this group of applicants, no one quite fits the bill, so there will be no callbacks. It's a time-consuming process, but Bailey has come to understand that careful hiring at the start avoids a lot of disappointments later.

By Wendy Zellner in Dallas

HIRING

At Southwest Airlines, the staff has grown by 97% in four years

Cover Story



Nucor

Rodney Mott, plant manager

Rodney B. Mott doesn't look like a top executive as he cruises along the shop floor at Nucor Corp.'s new steel mill in Hickman, Ark. But his hard-hat exterior is deceiving. The 43-year-old Mott, a former mill manager at U.S. Steel Group, is one of 21 plant managers whose surprising independence is at the core of Nucor's nimbleness.

There's no cumbersome bureaucracy at the Charlotte (N.C.)-based company. The agile steelmaker has decentralized decision-making so much that plant managers run almost every aspect of the business. Mott, for example, scours the world for his own raw materials. He also scouts out his own customers and sets his own production quotas.

give workers pay of about \$50,000 a year—about what unionized workers earn at other mills. But Nucor's productivity is far superior: At its Crawfordsville (Ind.) plant, it takes less than one worker-hour to produce a ton of flat-rolled steel, compared with an average of four worker-hours elsewhere.

To be sure, there's no guarantee today's hot-growth giants won't stumble later. Peters points out that Southwest and Wal-Mart, for instance, are relative youngsters alongside IBM, which took more than 70 years to flounder. And arrogance can develop more quickly than that—as demonstrated by Intel's initial high-handed treatment of its Pentium customers. Intel's 1994 profits were down less than 1% after a \$475 million charge for Pentium replacements. Says CEO Grove: "We have to learn some skills that are second nature to others."

Still, this decade could offer the best promise of growth

"Hickman operates like a separate company," Mott says. And he has a big say about when to expand. Last spring, he installed a second \$50 million caster, which turns liquid metal into bands of steel, nearly doubling the Hickman plant's capacity, to 36,000 tons a week.

That doesn't mean that headquarters isn't paying attention. Frequent phone talks with the central office are common. And almost every measurable aspect of each plant's performance is reported throughout the company. That, in turn, leads to plenty of competition among the plants. "There's a lot of little sibling rivalries going on," Mott acknowledges.

As his Hickman plant grows, so do Mott's responsibilities. His plant now supplies scrap and pig iron to other facilities. He is also scouting

out the Carolinas and Virginia for a good spot to build Nucor's next factory. All this strengthens Mott's hand within the company. He's among the favorites to become chief operating officer when Chief Executive F. Ken Iverson, 69, steps aside for his heir apparent, President John D. Correnti.

Perhaps with an eye to that possibility, a year ago Mott turned down the presidency of Gallatin Steel, a Kentucky startup. While the Gallatin position paid more money, he says, "I'd still be taking orders." That would be quite a change from

Nucor, where the usual advice Mott gets from his boss is "trust your gut." It's not always easy to do. But that's the way decisions get made at Nucor.

By Stephen Baker in Hickman, Ark.

MANAGEMENT

Nucor's
21
plant managers
handle
everything from
marketing to
production

that big companies have seen for quite a while, says Morgan's Prahalad. That's because of promising markets opening up abroad. Already, Motorola is making a big push along the Pacific Rim, especially in China, where it anticipates sales that will equal its American revenues by about the year 2000. And while their efforts in Latin America will be slowed by Mexico's meltdown, even Wal-Mart and Home Depot, whose focus is still mainly on U.S. expansion, are testing the international waters. Whether at home or abroad, though, the successful giants aren't likely to stray far from the lessons they have brought them this far. After all, speed, flexibility, and staying close to customers are skills that know no boundaries.

By Wendy Zellner in Dallas, with Robert D. Hofmann in San Francisco, Richard Brandt in San Francisco, Stephen Baker in Pittsburgh, David Greising in Atlanta, and bureau reports



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SPINNING ITS WHEELS: A '96 Caravan in a test chamber

AUTOS

HOW MANY REBATES CAN FIT IN A MINIVAN?

With sales flattening, Chrysler and Ford revive old tricks

When their fourth child arrived last summer, Cathie and Ken Zajac knew it was minivan time. Shopping at dealerships near their Philadelphia home, the Zajacs fell in love with the stylish, smooth-riding Ford Windstar. But that was before they eyeballed the \$24,000 sticker. "The price knocked us over," says Ken Zajac, 35, national sales manager for a sports news service. The couple quickly retreated to used-car lots and in January plunked down \$17,000 for a 1994 Dodge Grand Caravan.

The Zajacs aren't alone. For the first time in more than a decade, the torrid growth of sales for new minivans has suddenly slackened off. The reasons are varied: higher prices, competition from sexier sport-utility vehicles, and family budgets squeezed by climbing mortgage payments. The result has been bloated inventories. In late January,

Chrysler Corp. and Ford Motor Co. announced rebates of as much as \$1,100 on minivans. And Ford even shuttered its Windstar factory for a week. "They've hit a wall," says Salomon Brothers analyst John V. Kirnan.

BAD TIMING. Startled carmakers are staring at the prospect of squeezed profits on one of the industry's biggest money-makers. Although minivan sales are still expected to grow slightly this year, to about 1.3 million, analysts are dialing

back their previously bullish forecasts and now say manufacturers will need to keep juicing up rebates and other sales incentives to entice consumers. Ind. Chrysler Chairman Robert J. Ton recently conceded that cost of such incentives—wreached a low of \$410 per vehicle in the fourth quarter—would this year.

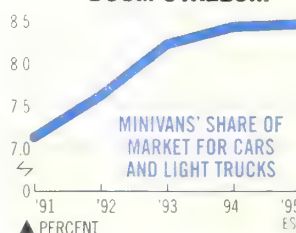
The slowdown couldn't hit worse time for the No. 3 carrier, which rakes in as much as of its profits from minivans. April, Chrysler will start selling its first brand-new minivan since creating the segment in 1983. 1996 models, which the company spent \$2.3 billion to develop, like they'll be a hit. People wait in long lines for a chance to see them during their first public appearance at Detroit's annual January show. The minivans are roomier, more stylish than the old models, boast neat new features, such as optional sliding rear door on the driver's side.

ROBBING PETER. But launching a vehicle into a tepid market is always a challenge. Moreover, the slump complicates the delicate process of clearing out older models to make way for the new. Just ask Ford. The company decided to continue selling its older, \$18,000 Aerostar model alongside the Windstar, which starts at \$20,000. But dealers the Aerostar has been stealing so cost-conscious buyers away from the newer model.

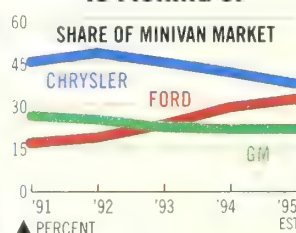
To try to avoid a similar blow, Chrysler's marketing honchos plan to phase out 1995 vans in stages, as production of the new 1996 model ramps up. The company has already stopped building the top-end Chrysler Town & Country and loaded versions of the Caravan and Plymouth Voyager. Chrysler

slapped the biggest rebates of \$750 to \$1,000, on those models. If all goes well, most of those Voyagers and Caravans will be sold by the time the end versions of the new models arrive at dealerships this spring. Meanwhile, Chrysler is still assembling the low-priced versions of the new model. Later this year, however, the company may be forced to sweeten the current \$500 rebates on these vehicles.

AS THE MINIVAN BOOM STALLS...



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to make way for their replacements.

If Chrysler's transition stumbles, Ford is poised to pounce on any weakness. After the Windstar debuted, Ford gained 6 points of minivan market share in 1994, while Chrysler lost 3.5 points. And this year, the No. 2 carmaker is eyeing more sales: Chrysler will build at least 65,000 fewer minivans as it shifts factories over to production of the new model. To keep the heat on, Ford matched Chrysler's giveaways with a nationwide \$1,000 rebate on the Aerostar and more than doubled the Windstar's markdown, to \$1,100. "We think we have the bases covered," says Keith Bins, marketing plans manager for Ford's minivans.

STICKER SHOCK. With penny-pinching consumers such as the Zajaacs out there, Chrysler's biggest potential pitfall may be pricing its new van too high. The company already increased stickers over the past year by about 5%, with the base model rising a hefty \$1,341, to \$16,160. Company officials say entry-level prices for the 1996 models will rise only enough to offset the addition of standard antilock brakes, now a \$600 option. "We aren't going to abandon that end of the market," says Richard A. Winter, general product manager for the minivan platform team. Loaded top-end versions, such as the Grand Voyager LE, which currently starts at \$23,680, will increase more, he concedes.

Still, if customers dig in their heels against higher prices and the rebate game really gets nasty, Chrysler has an advantage. Because its costs are lower, Chrysler now earns an average gross profit of about \$6,000 on its vans, estimates Kirnan. At Ford, it's more like \$4,500 to \$5,000, while General Motors Corp., which lacks a strong entry, is barely breaking even, Kirnan says. Moreover, since Chrysler's new van has 1,000 fewer parts than the one it replaces and thus is easier to build, profits could jump to an average of \$7,000 per van once production is up to full steam. That means Chrysler can afford to squeeze its competitors with fat marketing incentives and still turn a nice profit.

In the next few months, Detroit's marketing moguls hope their rebates, along with dollops of marketing hokum in the traditionally strong spring selling season, will bring back the good times. So do dealers such as Alan Spitzer, whose 22 retail stores in Ohio and Florida posted a 30% drop in minivan sales in December. Nor is January looking too hot. If that kind of sluggishness persists, the auto makers may have to concede that their high-profit minivan joyride is starting to run out of gas.

By David Woodruff in Detroit

The Corporation

STRATEGIES

PENNZOIL SWITCHES ON ITS SEARCHLIGHT

It's forsaking dealmaking to focus on oil exploration

Days after Thomas M. Hamilton took charge of Pennzoil's oil-exploration unit in 1991, he knew he was in trouble. Almost every geologist had been laid off or quit, leaving few promising fields. The company was looking frantically for acquisitions to maintain reserves. And instead of trying to cap the problems, Pennzoil's managers bucked responsibility up the line, sending Hamilton a two-foot stack of field-by-field drilling reports every Friday morning. "What do I want these for?" he finally snapped. "The last thing I should be doing is sitting in Houston telling our operators how to run their fields."

Yet that's just what Hamilton had to do. Decades of dealmaking by founder J. Hugh Liedtke had vaulted Pennzoil to near-major status, but the steady buying camouflaged mediocre performance at finding and developing oil and gas reserves. Worse still, the legal maneuvering surrounding Liedtke's crowning achievement—the \$3 billion 1988 settlement from his courtroom victory over Texaco Inc. for busting his proposed takeover of Getty Petroleum Corp. in 1983—had caused management virtually to neglect day-to-day operations.

"NEW BALL GAME." Now, Chief Executive James L. Pate, who succeeded the retiring Liedtke as chairman last May, is trying to make Pennzoil as effective a prospector in the oil field as it has been in the courtroom. A soft-spoken former economist who came to Pennzoil in 1976



after a Commerce Dept. stint in the Ford Administration, the 59-year-old Pate has sold off laggard units and strengthened the company's balance sheet. Most important, he has put Pennzoil back on the exploration trail, spending \$255 million since 1992 on ambitious plans to develop new fields abroad. With cash short and rivals restructuring, too, skeptics say Pennzoil still has a long way to go. "They have cut costs, but so has every oil company," says Bear, Stearns & analyst Frederick P. Leuffer Jr. "Whether Pennzoil is improving relative to the industry remains to be seen."

Certainly change was needed: 15 years after its windfall, Pennzoil has

show. Roughly \$350 million went to the Purolator oil-filter business—sold for \$206 million. With an addi- \$2.2 billion, Liedtke bought a 9.5% in Chevron Corp. By 1992, Penn- aded half its Chevron shares— worth roughly \$1 billion—for 139 oil fields in the Gulf of Mexico. ouble reserves, but performance as lackluster. Analyst Robin Shoe- of Lehman Brothers Inc. esti- that operating earnings for 1994 t \$289 million on sales of \$2.5 bil- less than the \$328 million Pennzoil d in 1991 on similar sales. e has wasted little time cleaning oil's slate. In October, he O. K'd a

To get there may take more hard choices. Although Pennzoil's debt-to-cap- ital ratio should fall from 66% to 52% by 1998—when Pennzoil's remaining \$900 million in Chevron shares will be swapped to reduce debt—the improved balance sheet masks another problem: Operating cash flow isn't enough to meet capital investments and the \$120 million dividend. Although asset sales and new equity made up the difference in the past, Leuffer expects Pennzoil's cash-flow shortfall to top \$350 million for 1994 and 1995—even though capital spending abroad fell to \$28 million last year. "Their capital needs are in- creasing, and they don't have the money," says Leuffer. "They can't afford that dividend."

But Pate insists re- building performance will be enough. Im- proving returns at Pennzoil's \$900 million oil and gas business will be vital; with roughly one-third of revenues and earnings, it's the key to the com- pany's future. Liedtke counted on inflation and high crude prices to keep asset values and deals rising—and dismissed an explora- tion staff that he thought unnecessary. "But the environment has changed dramati- cally," Pate says. "Now operational per- formance is everything."

Pate's game plan is simple: Squeeze more production out of ex- isting fields while sell- ing off less promising properties to fund long-term exploration. For now, Pennzoil is concentrating on over- seas sites such as Azerbaijan and Qatar. Down the road, new technology could also unlock huge reserves deep in the Gulf of Mexico.

PENNY-PINCHING. Ham- iltan, a well-regarded former head of British Petroleum Co.'s inter- national exploration ef- fort, has made some progress. Pennzoil's costs for finding and developing a barrel of oil topped \$8 in 1989, while U.S. majors spent around \$5. By selling the least pro-

ductive sites and trimming the portfolio from 800 fields to 500, Hamilton has lowered costs to \$5.40. Now, he aims to cut that to \$4.35.

At the same time, Pennzoil must re- build shrunken reserves; in recent years, it has replaced just 60% of annual pro- duction with new reserves. In 1994, new drilling boosted reserves slightly, to 448 million barrels of oil. More improvement should come from the long neglected fields Pennzoil bought from Chevron. Take the South Marsh Island gas field 80 miles off the Louisiana coast. Early last year, Pennzoil replaced eight aging struc- tures with a 1,200-ton platform. The \$70 million investment is paying off: New wells and more modern technology have increased production from 15 million cubic feet of natural gas per day last year to 95 million cubic feet today.

Hamilton is also trying to create a more decentralized, operations-oriented culture. To increase flexibility to cope with volatile crude prices, he wants field personnel to make cost-benefit trade-offs on-site—such as whether to fix damaged wells if prices don't justify the invest- ment. Still, tales of penny-pinching are easy to find in the Oil Patch, where 500,000 jobs have been lost in a decade. "Pennzoil is doing the same things as everyone else, only later," says a pro- duction manager at one rival. "They do a good job on their high-priority fields but have been pretty neglectful of others."

CRITICAL SALES. Pennzoil is also a late- comer to the global oil scene. While it has signed deals to develop fields in Qa- tar, Egypt, and Azerbaijan, overseas barrels are less than 1% of its total. Without the financial or technical muscle of the majors, "it's a difficult call as to whether they'll be successful overseas or not," admits retired board member Douglas J. Bourne.

Other problems could also crimp Pate's plans. Warm weather has slashed natural-gas prices and cut the value of fields, hurting efforts to sell \$250 million worth of domestic properties this year. If those sales are delayed, cash could quickly dwindle—forcing Pate finally to cut Pennzoil's dividend or trim devel- opment spending. But Pate says the dividend will stand. "I'm not saying

there won't be nega- tive cash flow next year—or even the year after that," he says. "But we're going to do what's needed to get our growth machine going." So long as Pennzoil wins no more landmark lawsuits, it might get there.

*By Peter Burrows
in Houston*

PATE HAS POLISHED PENNZOIL...

- Sold ailing businesses and refocused compa- ny on three key areas: motor oils, oil and gas exploration, and Jiffy Lube oil-change outlets.
- An October settlement with the IRS ends 12 years of legal wrangling over Texaco. With the Getty-Texaco affair behind it, Pennzoil can concentrate on improving operations.
- \$303 million in new equity, restructured debt, and a \$500 million write-off last fall give Pennzoil its strongest balance sheet in years.

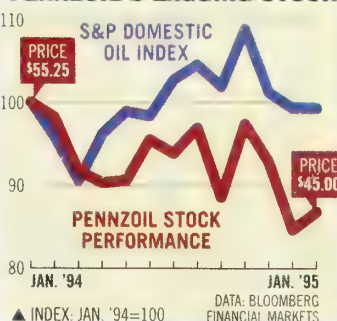
...BUT FACES A GUSHER OF CHALLENGES

- Company has little foreign presence. Penn- zoil must boost motor oil sales abroad and prove it can develop new fields in Azerbaijan and Qatar as cost-effectively as more experi- enced rivals.
- Pennzoil must shrink exploration costs and hike production from aging oil fields. Other- wise, cash to fund hefty dividends and ambi- tious foreign exploration will dry up.
- After years in which oil exploration lagged behind dealmaking, Pate must create a more decentralized, operations-oriented culture.

million write-down that included thing from back taxes on the Texa- tlement to losses on the sale of a -mining subsidiary and bad real -estments. That scarred 1994 re- Shoemaker expects net earnings tining operations to plummet 70%, t \$24 million. Yet even excluding me events, Pennzoil's net margin, at well below the industry average of Still, disgruntled investors, who ed Pennzoil's stock sink from 97 in to 45 today, applauded. "It's a new game now," says analyst Alan D. s of Gaines Berland Inc. "Pennzoil o back to being an exploration com- rather than a litigation company."

seas sites such as Azerbaijan and Qatar. Down the road, new technology could also unlock huge reserves deep in the Gulf of Mexico.

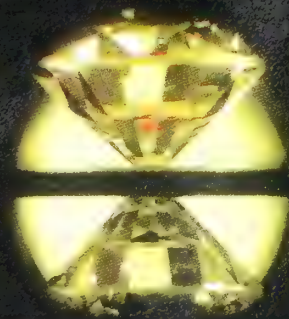
PENNZOIL'S LAGGING STOCK



MATERIALS

THE BIG SQUEEZE IN THE LAB

How extreme pressure is creating exotic materials



CRUNCH TIME: A DIAMOND ANVIL

In 1987, C. W. (Paul) Chu of the University of Houston was racing scientists from Moscow to Long Island for a breakthrough in high-temperature superconductivity. On a hunch, he prepared a bit of copper, barium, lanthanum, and oxygen smaller than a BB. Then he worked high-pressure alchemy, squeezing it under pressure 18,000 times as great as that at sea level.

Bingo: When electrodes were plugged in to the blend, it conducted electricity with zero resistance. Chu then guessed he could achieve the same effect at ordinary pressure by substituting yttrium for lanthanum. The substitution worked—and earned Chu worldwide fame for a material that superconducted at a record high temperature: at -180°C .

Chu's work highlighted how extraordinarily high pressures can strong-arm elements into yielding their secrets. The

high-pressure manufacture of synthetic diamond (by squeezing carbon) is already a near-billion-dollar industry. Today, researchers are using pressures exceeding those at the center of the earth to break and re-form chemical bonds in everything from hydrogen to beach sand. "Even by a conservative estimate, we could triple the range of materials we now know just by squeezing them," says Robert M. Hazen, a research scientist with the Carnegie Institution's Geophysical Laboratory and author of a 1993 book on the topic, *The New Alchemists*.

If gases can be compressed into stable metallic crystals they might superconduct even at room temperatures. Superhard glass made from silicon dioxide—or quartz—could serve as windshields for rockets. A metallic form of hydrogen could be an incredibly dense form of stored chemical energy. "It

would be something like 30 times more efficient than any existing rocket fuel," Hazen says.

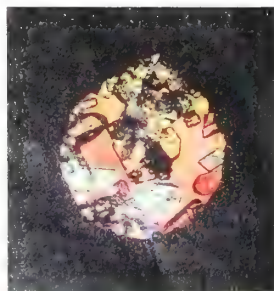
The laboratory equipment required to achieve these awesome pressures, a diamond anvil, is no more than 8 inches tall and can be screwed tight by hand. It works by amplifying arm pressure through gears and concentrating all of it into an extremely small area. This is done by placing a tiny sample between the tips of two cut diamonds. A pressure with a hole in it corrals the sample.

Research on such a small scale has big drawbacks. The products are tiny—about a millionth of an ounce—to be useful for anything except research. Many materials revert to normal once the pressure is off. And high-pressure science can be hazardous. Hazen witnessed one explosion, David Mao and Russell Hemley of the Carnegie Institution now operate experiments from behind a steel wall.

With real money probably years away, most work on exotic high-pressure materials is going on in universities and companies. Cornell, Harvard, and the University of California at Berkeley have substantial programs. Three years ago, the National Science Foundation established a Center for High-Pressure Research, pooling efforts at the Carnegie Institution, Princeton, and the State University of New York at Stony Brook.

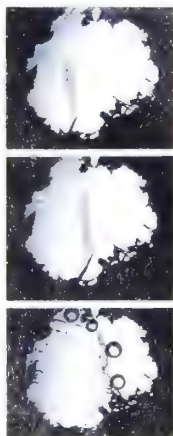
HARD LUCK. High-pressure research got a jolt last May when 11 Russian and French researchers claimed in the journal *Physics Letters* that they had created a material harder than diamond from "buckyballs," or carbon-60. But some claims have arisen before, and some scientists argue that the samples were small to be reliably tested.

Squeezing materials does more than harden them. Compressing gases such as hydrogen liberates their electrons, turning them into excellent electrical



PHASE SHIFT

Ikaite, top, and three views of helium nitride under pressure



HIGH-PRESSURE ALCHEMY

It's not just making diamonds from graphite: All kinds of ordinary materials take on startling characteristics when subjected to extremely high pressure.

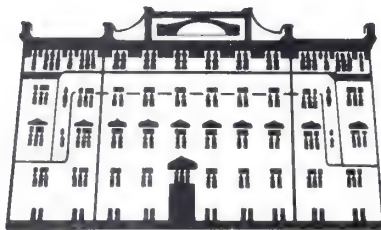
MATERIAL	POTENTIAL USES
HYDROGEN, OXYGEN	Fuel cells, superconductors
CARBON-60, OR BUCKYBALLS	Coatings for computer disks, abrasives
SILICON DIOXIDE	Superhard glass, lightweight car components
IKAITÉ	Indicator of how mineral deposits form
HELIUM NITRIDE	Aid to research on inert gases

DATA: CARNEGIE INSTITUTION; BUSINESS WEEK



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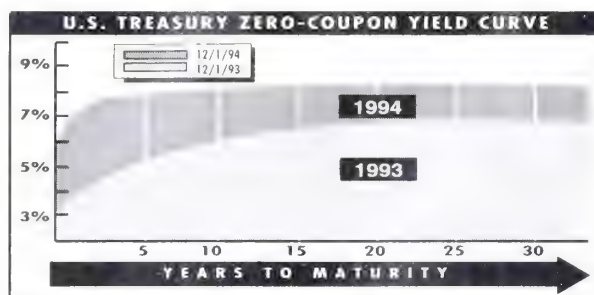
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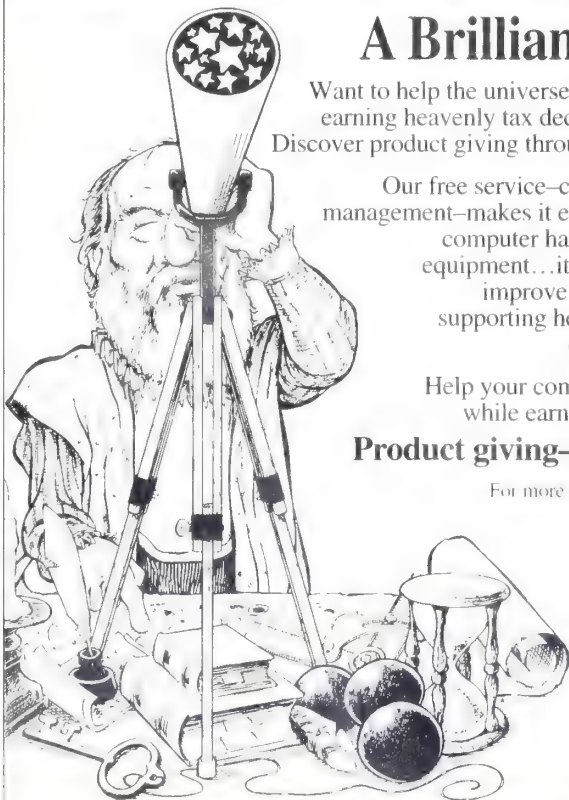
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conductors. Helium, ordinarily inert, forms a bond with nitrogen when sufficiently compressed. Oxygen is ordinarily colorless—but under extreme pressure forms crystals with facets of red, yellow, and blue. UCLA professor of physical chemistry Malcolm F. Nicol speculates that sulfur crystals could store information, with different colors of light serving to write, erase, and read.

The quest for a superconducting metallic hydrogen is taking scientists into realms of pressure never experienced on earth—and into heated rivalries as well. Researchers at Harvard University and Carnegie Institution disagree over what happens to hydrogen at a million atmospheres, or megabars, which point its molecules line up like watermelons. Carnegie brags it was the first to reach 2.5 megabars. No one has surpassed 3 megabars, where scientists speculate hydrogen becomes fully metallic and superconducting. The big question: Will metallic hydrogen remain metallic once the pressure is off?

MICROPOPS. Commercialization is one goal. High-pressure researchers seek to understand the composition of stars and planets and the source of earthquakes. UCLA's Nicol has even created conditions of the early earth, where long chains of hydrogen cyanide, which he believes are precursors to DNA, are formed. His favorite for research is ikaite, a white calcium compound. Its behavior under high temperature and pressure sheds light on how veins of gold, silver, and other ores are formed. Raymond Orloff, a physicist at UC Berkeley, and graduate student Charles Meade proposed a new seismic theory after visualizing serpentine, a greenish mineral. A microphone attached to a diamond anvil picked up a popping sound—perhaps a miniature version of a quake that occurs when water is forced out of serpentine deep underground.

Doubts about the commercial value of exotic high-pressure materials have kept them away from mainstream producers of synthetic diamonds, such as General Electric, Sumitomo, and De Beers. "We're a materials supplier. Just creating high-pressure phases doesn't make you any money," says William F. Banholzer, manager of engineering for GE Superabrasives in Worthington, Ohio. But in labs like that of Chu's, the big squeeze is paying off. He recently found a superconductor that he hopes could be produced in industrial quantities by depositing the material in vapor form. That's the kind of advance that keeps the pressure on.

*By Ruth Coxeter, with Peter Coxeter
New York*

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EDITED BY OTIS PORT

A PLACE IN THE SUN FOR WASTE SILICON?

FOR YEARS, SOLAR-ENERGY proponents have championed silicon—the stuff of computer chips—for turning sunshine into electricity. Trouble is, the cost of this form of silicon power is much higher than volts from fossil-fuel generators. But scientists at Oregon State University's Center for Advanced Materials Research are working to change that, using a

tough transparent cement.

With this high-tech glue, the scientists want to build durable solar panels by mixing waste silicon from chip-making plants into the cement. The approach should be much cheaper than using new silicon to make the panels. In fact, the semiconductor industry might pay to have its scrap silicon ground up for plastic cement. Some 10,000 tons of

toxic silicon waste are produced in the U.S. Using it all to generate electricity, OSU figures, could match the output of eight nuclear power plants. One clever concept would put a silicon tile on railroad ties. Each kilometer of track would then produce 100,000 watts. John R. Arthur, an OSU professor emeritus who directed the materials center until Jan. 1, says ironing out the wrinkles may take about two years.



THESE BOTTLES NAG YOU TO TAKE YOUR MEDICINE

WITH TODAY'S HUGE ARSENAL of drugs, doctors can combat diabetes, glaucoma, hypertension, and dozens of other diseases. But they can't get people to take their medicine. Forgetful and reluctant patients rack up \$25 billion in avoidable hospital bills each year, according to the National Pharmaceutical Council. Reston, Va., plus billions more in unnecessary nursing home admissions.

One remedy may be the medicine containing themselves to remind patients when it's time to take a pop. Apex Corp. in Belmont, Calif., builds a "smart" bottle cap that's equipped with its own chip, a clock, and a tiny display. The cap keeps track of how many times the bottle is opened and can nudge patients with electronic beeps.

Now, Apex has added a modem that reads the patient's memory and automatically relays to Apex the number of times the cap was moved that day. If the clock isn't right, the patient gets a reminder call in the morning. The service, called SmartCap Partners, costs less than \$2 a day—but isn't covered by insurance. Still, Apex has drawn some big backers. Last fall, Pfizer invested \$1 million to join Johnson & Johnson and New York University as an equity partner.

SUPERCOMPUTERS THAT LITTLE GUYS CAN BORROW

FOR SMALL COMPANIES TACKLING a monster-size science or engineering puzzle, supercomputer power is now just a modem call away. Sandia National Laboratories has inaugurated a new business connection called Technology Information Environment for Industry, or TIE-In. The service shortcuts the usual federal red tape. Gaining real-time access to Sandia's awesome computer horsepower requires just a pat, two-page agreement.

Alliant Techsystems Inc. is the first customer to link up. To help the Minneapolis company, Sandia shoots objects into window glass, then X-rays the glass to see how it was affected. As soon as the raw data are captured, Timothy J. Holmquist, a researcher at Alliant Techsystems, can begin analyzing the results from his office in Minnesota. TIE-In labs specialize in areas ranging from welding and environmental information systems to structural analysis and virtual prototyping of manufacturing processes.

MAYBE IT IS EASY BEING GREEN

DOES IT PAY TO BE GREEN? PIONEERS SUCH AS DUPONT, Dow Chemical, and Procter & Gamble have insisted for years that they reap big savings by preventing pollution instead of trying to control emissions after the fact. Still, the notion that pollution prevention is a financial boon has plenty of doubters.

Now, a study by Stuart L. Hart, director of the corporate environmental management program at the

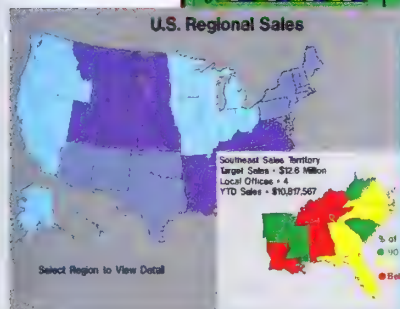
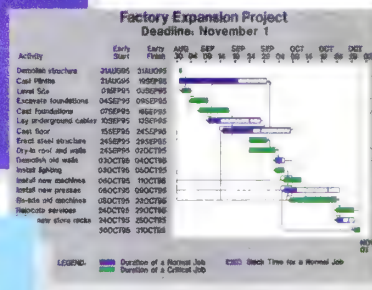
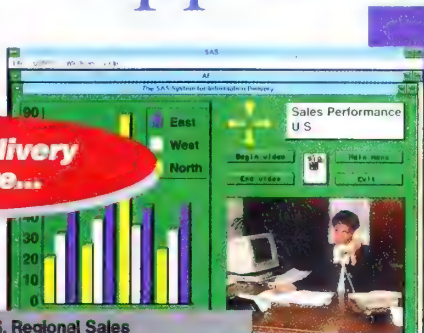


University of Michigan-Ann Arbor business school, makes a strong case for pollution prevention. Hart did a statistical analysis of the effects of pollution cutbacks in 1988 and 1989 on financial performance from 1988 to 1991, using 127 companies from the Standard & Poor's 500-stock index. After accounting for variables such as research and development intensity and size, his findings show that operating performance began to improve within the first year—and by the second year, pollution prevention was lifting return on equity, too. Of course, the biggest polluters benefited most, since they had plenty of low-cost opportunities on hand.

Based on this work, Hart believes most companies could slash emissions as much as 70% before hitting a point of diminishing returns. But since that might take 10 years, improvements in technology could mean that what isn't cost-effective today might be by then.

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WHY INVESTORS STAMPEDE

...And why the potential for damage is greater than ever

This, too, shall pass.

If every trader and investor remembered that aphorism, the financial markets would be far different. But time, experience, and information haven't made people any the wiser. Whatever the spark, when the markets ignite, a flash fire can still easily turn into a firestorm. Traveling up or heading down, the markets habitually take on a momentum of their own, and prices end up "overshooting," or reaching extreme highs or lows before settling back. It's as true today as it was when the stock market crashed in 1987—or 1929.

The panic over Mexico is a case in point. For the past few years, money surged into Mexico, buoying the *bolsa* and helping to finance short-term borrowing. Political unrest and the assassination of a presidential candidate in 1994 barely dimmed investor enthusiasm. Then, a surprise yearend devaluation stunned the markets. In the following weeks, the peso plunged, dragging the value of Mexican stocks and bonds down. Only a U.S.-organized rescue appeared to stop the carnage. It may be some months before it's clear to what extent prices overshot, but in a few weeks, the peso had lost more than 50% of its value against the dollar, putting it well below purchasing-power parity. How could this happen? How could Mexico go from being an investor darling to dog so quickly—and carry so many other emerging markets down with it?

Easily. At times like these, the markets are propelled largely by psychology. As bandwagons form, investors' herd instincts frequently push prices far beyond where they ought to go. Yet psychology can turn on a dime as new information or news events are absorbed, sending prices off in the opposite direction. This is even truer during a currency crisis than during a market crash, because foreign investors who face massive exchange losses are frequently hostages to indecisive policymakers.

Speculative bubbles and crises of con-

fidence are not new, of course. But the potential for financial and economic dislocation is greater than ever. That's because the growth, sophistication, and leveraging of financial markets around the globe has enabled investor psychology to have swift and powerful effects. A wide array of new securities, from collateralized mortgage obligations to emerging market debt, beckons investors. Pension funds and mutual funds have ventured into new worlds of investment. At the same time, high-speed transmission of information and trades makes it easy for hedge-fund managers and pensioners alike to move in and out of markets at will. In today's global markets, there are no fire walls.

CASCADES. Investor behavior is still a murky area for economic research. By now, though, economists and psychologists have concluded that the most important factor influencing investor behavior is the recent past—recent news, recent earnings or, for that matter, recent trends in the markets. That means earnings prospects or economic fundamentals count for little, while "this week's bad news carries far too much weight," says Richard H. Thaler, economist at Cornell University.

The tendency to see the recent past as prologue is amply demonstrated in surveys of market participants' views before, during, and after the crash of the Nikkei 225 at yearend 1989. Reporting the results in a recent paper,

When Markets Overshoot

Identifying overshooting while it occurs is difficult. But after the fact, periods of jubilation and panic are clearly identifiable. Here are some examples:

1984-85 DOLLAR SURGE

The U.S. dollar had been climbing since 1981, buoyed by high real rates of interest. Widening trade and budget deficits should have stalled its ascent, but speculative buyers pushed it higher until the Plaza Accord in September, 1985.

1987 U.S. STOCK MARKET CLASH

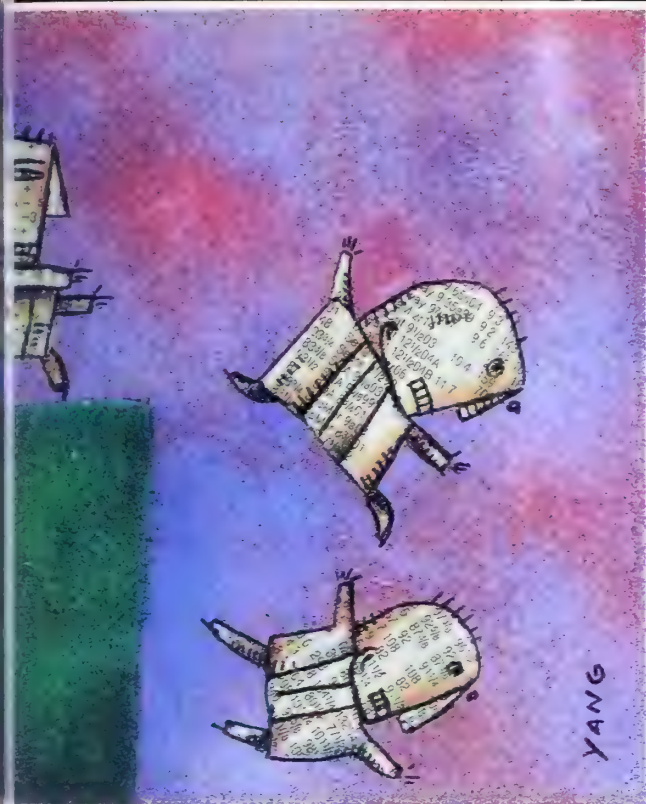
The U.S. bull market began in August, 1982, as the economy rebounded and corporate profits grew. Rates started rising in the spring of 1987, with rates moving toward double digits, but stock prices kept on climbing.



Robert Shiller of Yale University, co-authors Fumiko Kon-Ya of the Pan Securities Research Institute, and Yoshiro Tsutsui of Osaka University found that large numbers of investors ignored warnings that the market was becoming more and more overvalued.

Indeed, just before the crash, 48% of the Japanese respondents thought that if prices dropped 3% in one day, the market would nonetheless rise the next day. "This impression of stability in the market may have encouraged high prices that the Nikkei reached before the crash," the study says.

The Nikkei, much like the Dow Jones years before, crashed for no apparent reason—there was no major event or economic occurrence that precipitated the break in prices or could adequately explain it. But economists call "informational cascades" may explain both how investors can get caught in speculative bubbles and when markets gain speculative momentum.



The central influence on investor behavior is the recent past, say psychologists. Long-term prospects or economic fundamentals count for little

agers gingerly tested the waters with small purchases of American Depositary Receipts, which had gotten especially hammered. But it took a massive rescue program to turn things around.

By their very size and design, the markets have encouraged fickle behavior. Look at the ease with which capital has flowed across borders and pumped up the growth of new markets. Since 1989, says David D. Hale of Kemper Corp., private capital flows to emerging stock markets in Latin America, Asia, and Africa have expanded from less than \$10 billion a year to between \$60 billion and \$80 billion a year. Meanwhile, the combined stock market capitalization of those regions now exceeds \$2.1 trillion, says Hale, compared with only

and how bubbles can burst. Economists Ivo Welch, Sushil Bikhuni, and David A. Hirshleifer of University of California at Los Angeles argue that people typically observe the behavior of their peers, or they are choosing a restaurant investment. Even if their own intent may run contrary, when they see that their peers favor something, they tend to go with the herd and justify their decision by reasoning that the consensus of opinion must be correct. This leads to an informational cascade, with people observing and following their peers. Such lemming-like behavior is understandable. It takes an awfully big ego to stand one's ground against a tide of opposing opinion. "No one is stupidly," says Welch.

Despite their apparent power, these herds can shift suddenly in the opposite direction with just a few pieces of information—or because just a few peo-

ple decide to change course. In fact, a look back at the period just before the 1987 crash in the Dow indicates that money in the options market was anticipating a sharp decline. Similarly, when the dollar was still climbing in 1984-85, six-month forward rates pointed to a dollar decline, even though one-month forwards showed strength.

It's generally the smart money, the so-called "stabilizing speculators," who step in when prices have been driven to unexpected troughs or who exit soaring markets before outrageous peaks are reached. In the case of Mexico, such investors were scarce—too scarce to set off cascades. One small hedge-fund manager, figuring the markets had overreacted in early January, bought short-term dollar-denominated Mexican paper, or *tesebonos*, in the secondary market to yield 30%—a good bet, given that Mexicans sold such paper at auction with yields of 20% a week later. Some portfolio man-

\$400 billion 5 years ago and barely \$100 billion 10 years ago. And when money flows to emerging markets through unregulated mutual funds rather than through regulated banks, says Albert M. Wojnilower, senior economic adviser at CS First Boston Investment Management Corp., that money is sure to be far more volatile.

"INVOLUNTARY DUMPING." So the January tumble in Mexican securities—and the contagion that spread to other Latin markets—was not merely a matter of psychology. What began as an understandable sell-off picked up speed because scores of portfolio managers at mutual funds and pension funds had no choice. They had to worry about near-term performance and about meeting investment criteria. And mutual fund managers had to worry about the prospect of massive redemptions. "There was a lot of involuntary dumping and forced selling," observes Robert W. Vishny, an economist at the University of Chicago.

In this age of near-perfect information and highly competitive markets, investors aren't supposed to overreact and prices aren't supposed to overshoot. Any "mispricing"—that is, any price that doesn't accurately reflect value—should be quickly traded away by investors seeking to capitalize on the market anomaly. But overshooting and overreaction continue to occur. Given human nature and the vast and sophisticated markets that people can play, that's not likely to change anytime soon.

By Karen Pennar in New York

U.S. STOCK MARKET CRASH

Indexed 508 points in 1987. Within a year, however, prices tumbled at year-earlier rates and the market fell sharply. By August, 1989, the market had turned to its pre-

1989-90 JAPANESE STOCK MARKET CLIMB

The Nikkei 225 also started climbing in 1982 but withstood the shock from Wall Street. It ascended rapidly, reaching a peak at yearend, 1989. Prices tumbled over the next couple of years and remain below the 1989 peak.

1994-95 MEXICAN MARKET PLUNGE

Mexico was buoyed by a surge of foreign investment in 1992 and 1993. Political unrest worried some investors in early 1994, but it was the surprise devaluation of the peso on Dec. 20, 1994, that spawned a panic.

MUNICIPAL FINANCE

WILL MERRILL TAKE A HIT IN ORANGE COUNTY?

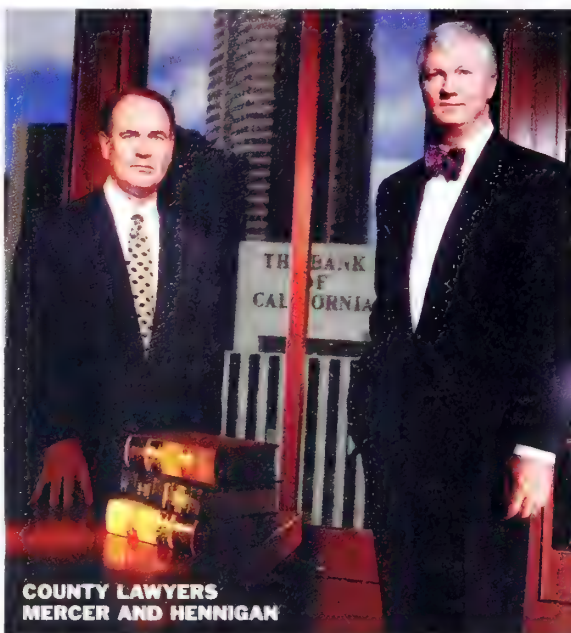
An arcane legal twist could stick the firm with part of the tab

The similarities are striking. Back in 1984, the city of San Jose, Calif., sued several major brokerages it blamed for some \$60 million in investment losses. Faced with a weak legal position and the prospect of millions in litigation costs, all but two of the brokers settled for a total of \$24 million without admitting or denying guilt. Among those who mailed in their checks was securities giant Merrill Lynch & Co., which ponied up \$750,000.

Merrill could be stuck with a vastly larger tab when the dust settles on a similar dispute with Orange County, Calif., which filed for bankruptcy on Dec. 6 because of \$1.7 billion in losses from risky derivatives investments. Merrill, in effect, lent the county's investment pool more than \$1 billion to leverage up its portfolio. On Jan. 12, the county sued Merrill, seeking upwards of \$2 billion in restitution for transactions the firm allegedly knew exceeded the county's authority and were part of an unwise investment strategy. Merrill blames County Treasurer Robert L. Citron, who ran the investment pool.

BEYOND THE PALE? The case, though, is likely to turn on some arcane legal issues that put Merrill at a distinct disadvantage. Several lawyers contacted by *BUSINESS WEEK* bet that Merrill will agree to take a big hit to avoid protracted litigation. "My instinct is that Merrill Lynch will have to settle this case," says University of Southern California law professor Jennifer H. Arlen. Some guess Merrill could end up paying more than \$100 million.

No way, says Merrill. "I think we will win this case on a motion long before you'll see a trial," says Dennis J. Block, a partner with Weil, Gotshal & Manges, which is representing Merrill.



COUNTY LAWYERS
MERCER AND HENNIGAN

"We believe this case will be dismissed based on law and facts."

The crux of both the San Jose and Orange County cases is what are termed *ultra vires* actions—beyond the scope of a particular entity's legal power or authority. Orange County claims that Citron borrowed considerably more money, via repurchase agreements with Merrill and others, than was allowable under the state's constitutionally mandated limits on county debt. Repurchase

agreements are a form of collateral lending where one party sells securities and agrees to buy them back in the future at a higher price. Because Citron exceeded his authority, the county claims, the loan transactions were invalid, and Merrill should return to the county all collateral and interest. A recent court filing says the debt limits apply to the county's investment pool.

Although Citron almost single-handedly managed the pool for years, Merrill could have trouble arguing that Citron should take the blame for his actions. County lawyers, led by James M. Mercer and J. Michael Hennigan, assert that California requires contractors dealing with the state to know the intricacies of state law. Thus, Merrill should have known that Citron acted beyond his legal authority. Says Hennigan: "[Merrill Lynch's] investment scheme was illegal and contrary to California's statutes and constitution."

PRECEDENTS. The San Jose case could be a troublesome precedent for Merrill say attorneys. The U.S. district court judge ruled that the city's repurchase agreements—by which San Jose leveraged up its investment portfolio—were *ultra vires* because they were outside state investment guidelines. The ruling ruled against the brokers who refused to settle. Weil Gotshal's Block argues the case is not a precedent because of factual differences.

A circuit court judge in West Virginia ruled against Morgan Stanley & Co. in an earlier *ultra vires* case. In 1991, the state investment pool suffered \$225 million in losses. Morgan Stanley was one of many dealers who sold Treasury securities to the state. According to the judge, the transactions were inherently speculative and thus beyond the manager's authority. Most dealers settled and paid \$28 million. The judge levied a \$56 million judgment on Morgan Stanley, which is appealing the ruling.

"If Orange County were to win an *ultra vires* argument, they would win 75% of the way home on a large judgment," says University of California professor John C. Coatsworth. Yet a victory for either Orange County or Merrill on narrow legal technicalities still won't answer the larger question of who is to blame.

By Nanette Byrne
Los Angeles with
Nathans Spiro in
York

The Blame Game

ORANGE COUNTY SAYS:

Treasurer Robert Citron was misled by Merrill, his financial adviser, which lent more than \$1 billion to the county. Merrill should have known that Citron's leveraging of the county's investments exceeded the state-mandated ceiling on county debt. Thus, the firm should not have lent him money beyond that ceiling.

MERRILL LYNCH SAYS:

The suit is entirely without merit and will be dismissed. Merrill was not Citron's financial adviser and did not mislead him. Investment strategy, including leveraging the portfolio, was Citron's responsibility. The county debt limit does not apply to the investment pool that Citron managed.

DATA BUSINESS WEEK

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BY GENE G. MARCIAL

LOTTO FEVER COULD STRIKE HERE

Guess who's back on track? GTECH (GTK), and it's sprinting higher after a bad spill in early December. The stock of this leading worldwide operator and supplier of computerized lottery systems had slumped to a low of 16 late last year. But it has since resurged, shooting up close to its 52-week high of 23. That's remarkable for a company whose sales and earnings slackened last year because of increasing competition. So what's fueling the

WINNING NUMBERS?



recent flareup in GTECH's stock? Takeover talk.

International Game Technology (IGT), the dominant maker of coin-operated slot machines, is believed to be eye-balling GTECH. Analysts say the lottery system maker is worth 35 to 40 in a buyout.

One New York money manager who is close to management insiders at International Game says the slot-machine maker wants a friendly merger with GTECH, based in West Greenwich, R.I. The proposed deal, according to this investment pro, is a stock-cash swap transaction. But informal talks between executives in both companies have been stymied, said the source, because of the recent weakening in the price of International Game's stock—from nearly 24 in September to 13% on Jan. 31.

Still, a merger with International Game would be the logical move for GTECH, according to some analysts. "The fit and synergy between GTECH and IGT are perfect," says Michael Moe, an analyst at Lehman Brothers based in New York.

He explains that GTECH's earnings have been dragged down by its product-sales operations, which account for some 23% of total revenue. The services unit, however, which generates 77% of revenues, has been growing robustly, says Moe. But he notes that "IGT is exactly the reverse: Its service operations account for 25%, and product sales 75%." And while the lottery-system operator is big in the international markets, IGT is dominant in the U.S. but just starting to establish its foothold overseas.

The businesses of GTECH and IGT are so closely related that a combination would bolster their bottom lines, notes Moe, who says that based on fundamentals alone, GTECH "is a compelling buy." The stock is trading at only five times cash flow and continues to be an attractive "growth" play, argues Moe. And GTECH by far is the "dominant leader in the lottery market worldwide," he adds.

A spokesman for International Game Technology said the GTECH rumor was "pure market speculation." A GTECH spokeswoman said the company does not comment on market rumors.

HEINZ WOULD BE A SAUCY TARGET

To someone who makes a living picking stocks, there's nothing as sweet as bagging a few takeover targets. And that's what investment adviser Ignatius Teichberg has done over the years. Indeed, in his weekly market letter that he faxes to his clients at New York-based Brod Capital Management, he has documented some impressive takeover hits. Among the companies Teichberg predicted would be snapped up: American Cyanamid, Gerber Products, McKesson, Continental Bank, and Pet.

Teichberg's new pick is H.J. Heinz, the major worldwide food producer that has long been rumored as a takeover target. The food giant's products include ketchup, sauces, vinegar, pickles, canned tuna, as well as meat products, corn syrup, and pet food.

Teichberg notes that the food conglomerate's stock has been strong, climbing from 32 last summer to 40 in late January. And although Heinz management has consistently declined to make any comments about the takeover speculation, Teichberg claims that one source at the company

said Heinz would sell if the price is right. Teichberg figures the buy price could be 60.

Rumors are that the most interested suitor is Unilever. A spokesperson Unilever said the company doesn't comment on rumors or speculation. Heinz did not return phone calls.

IS BRISTOL-MYERS STALKING AMGEN?

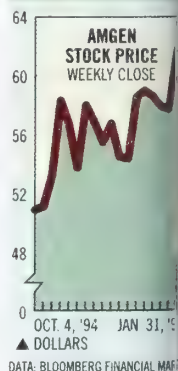
When Ciba-Geigy announced in November that it was buying controlling stake in Chiron, a frustrating game began: Which big tech company would be the next to over target? Some buyout pros think the answer is Amgen (AMGN), whose stock has risen from 55 in November to 63 on Jan. 31.

Investors believe the acquirer will be Bristol-Myers Squibb (BMY), one of the world's largest pharmaceutical companies. The betting is that Bristol-Myers will pay 90 a share for Amgen, one of the few biotech companies with successful products in a fast-growing market—and making fistfuls of money to boot. Its chief products include Eprex, which promotes the production of red blood cells, and Neupogen, which stimulates the production of white blood cells. Analysts expect Amgen will post earnings of \$3.10 for 1994 vs. 64¢ for 1993 and \$3.65 for this year.

Bristol-Myers, whose stock just hit a 52-week high, has been searching for a biotech company with proven products, says a California money manager who has been accumulating Amgen shares. Key Bristol-Myers products include the cardiovascular drugs Capoten and Corgard and anti-infection medicines Azactam and Cefzil.

As the world's largest biotechnology company, with 1994 estimated sales of \$1.6 billion, Amgen, which is based in Thousand Oaks, Calif., could prove a formidable rival to Bristol-Myers with the new product needs to maintain its leadership. Amgen declined comment.

THE BUZZ IN BIOTECH



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PRODIGY IS IN THAT AWKWARD STAGE

It's losing ground in the online race, but a radical redesign may soon come to the rescue

This should be the best of times for Prodigy Services Co. Suddenly, millions and millions of consumers are using their home PCs to vault into cyberspace—to browse for information, chat about their favorite topics, shop, trade stocks, take a dip in the vast reaches of the Internet. At last, a decade after Prodigy owners IBM and Sears, Roebuck & Co. made a daring bet on what had not yet been dubbed the Information Superhighway, Prodigy looks to be in the right place at the right time.

Maybe. But only if slick new graphics, a revised business and marketing plan, and a strategy to make Prodigy the most popular, most user-friendly gateway to the mysterious Internet succeed. Despite an early start in bringing a mass audience into the online world, Prodigy is rapidly losing ground. It's stuck too long with a clunky, dated interface, and worse, its big plans to generate profits from online shopping and advertising never paid off.

Meanwhile, America Online has leapfrogged Prodigy. AOL—which carries an electronic version of BUSINESS WEEK—is in a virtual dead heat with No. 1 CompuServe Inc. Both reach more than 1.6 million U.S. households, according to New York-based market researcher Jupiter Communications Corp. But Prodigy has remained relatively flat this year, at 1.35 million paying accounts. Despite cutting 550 jobs through attrition and two rounds of layoffs, the White Plains (N.Y.) company is still not profitable. And the outlook could dim later this year with the arrival of formidable new competition: Microsoft Network and AT&T's Interchange. "It's getting close to sink or swim for Prodigy," says Michael Rinzel, a Jupiter analyst.

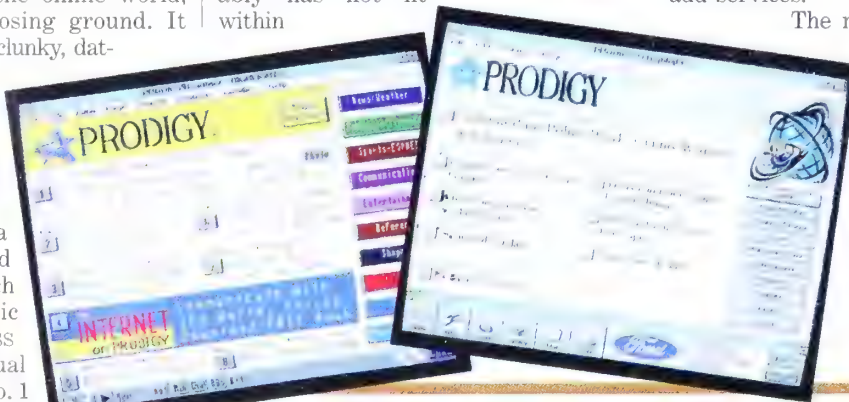
But Prodigy's backers are far from giving up. The partners have "been very consistent and supportive," says Prodigy President Ross S. Glatzer, dismissing recent rumors that IBM wants to buy out Sears. IBM won't comment, and both companies decline to discuss their plans for the venture. However, Prodigy execs say the current corporate structure will remain. Furthermore, Prodigy officials promise profits in 1995—on revenues of approximately \$200 million.

BILLION-DOLLAR BABY. It's not hard to see why Prodigy lost its way. IBM has been focusing on corporate customers, while Sears has sold or spun off most of its nonretail businesses. Analysts estimate that the pair has poured more than \$1.2 billion in—with nothing to show. "In the last several years, it probably has not fit within

the IBM strategy," admits IBM SVP Vice-President G. Richard Thomas.

Glatzer, formerly a marketing manager for Sears, may just have the plan to keep Prodigy in the race. Step One: Bring the Prodigy user interface into the '90s with a good-looking, easy-to-navigate design. Step Two: Instead of supporting costly and time-consuming efforts to develop its own services, Prodigy is aggressively wooing out content providers. Step Three: Sell the proprietary Prodigy technology, which made it slow and cumbersome, to create content for the network, and switch to industry-standard software such as the hypertext markup language (HTML) used on the Internet. That will take Prodigy out of the software development business and make it easier to add services.

The new Prodigy interface



FACE-LIFT

Prodigy's old graphics will be junked in favor of a slicker design that's also supposed to be easier to navigate.

The Best And Worst Of Times At Prodigy

SEPT. 1990 After three years of development, service begins. Aimed squarely at the consumer market, Prodigy was the first online service that featured a flat monthly membership fee and advertising.

SEPT. 1992 Its 2 million members are spending all their time E-mailing instead of shopping its online stores. Prodigy is forced to change to a more conventional pricing plan and begins charging for E-mail. Members start to revolt and head

for rivals CompuServe and America Online (AOL).

JAN. 1993 To reduce operating costs, Prodigy cuts 250 from its 1,100-member workforce, citing the need to "streamline the company." Major groups are consolidated and customer service outsourced.

NOV. 1993 The member revolt continues, and Prodigy begins to develop new areas and services. Live TV ads

ally code-named P2, is expected spring. More than just a pretty it is a complete reworking of the gy software. It will feature true tibility to Microsoft Windows and ple Macintosh, giving the service me "look and feel" of other Win- and Macintosh applications. What's important, however, is that now it providers—such as *Newsweek*— it up their services using common ry software rather than relying odigy technology. "Now, I can go d make services the way I want," Joshua Harris, president of Jupiter ctive, which is developing Prodigy s and "chat" areas that appeal to 1- to 30-something crowd.

THE BUILDER. Prodigy's boldest move, er, is its strategy to co-opt the et movement. "Our actual operat- ilosophy is to be totally intermin- with the Internet," says Prodigy resident Scott Kurnit. This month, gy became the first commercial e to offer a so-called Web browser ets subscribers tap into the World Web, the Internet's fastest-grow- ment. Some 110,000 folks have his feature, making Prodigy the popular way to reach the Web.

at's more, by moving over to a etely "open" system, Kurnit says, gy can become a service bureau, gy others to develop so-called Web and services—on the Internet or odigy. With its nationwide com- system and communications and systems, Prodigy could offer any t provider the opportunity to de- its own network. "If there are s that want to come on the Inter- s part of Prodigy or not—we will with them," says Kurnit.

re are risks to the Internet strat- or starters, the other services imilar Internet "gateways." And ole plan could backfire if custom- d they don't need Prodigy or any- se to help them onto the Net. Prodigy is getting credit for plot- plausible rebound plan. "Eighteen

woo back members who have ppointed with recent access at fast-rising rival AOL.

4 New features such as Inter- and slicker graphics help subscribers, but the venture produce a profit. Another yees are axed.

Prodigy Vice-President Scott s the company has been refocused and will introduce rface—dubbed P2—that fol- net standards.

months ago, they were in a bad position," says Mary Modahl, an analyst with Forrester Research. And now? "They are the sleepy company that has been goosed," she says.

In the past few months, Prodigy has come out swinging. In addition to offering the Web browser and popular chat features, there's a new online version

of the Yellow Pages for the entire Nynex region, and next month, a new kids feature called Homework Helper will debut. The result: Usage is up, say Prodigy officials. If the rest of Prodigy's efforts pay off, this could finally turn out to be the best of times.

By Paul M. Eng, with Ira Sager, in New York



ONLINE SERVICES

EUROPE ENTERS THE CYBERSPACE RACE

And a battle is brewing between U.S. and homegrown services

With rare exception, the history of computer markets has been that whatever happens in the U.S. will play out a year or two later in Europe. That would make 1995 the year Europeans go online en masse—following the lead of stateside consumers. In the U.S., membership in services such as America Online, Prodigy, and CompuServe jumped from 3.13 million to 5.36 million in 1994, according to market researcher SIMBA Information Inc.

Sure enough, the battle for Europe's net surfers has begun. After taking an early lead with Minitel, the pioneering electronic information service that France Telecom gave away to all French phone subscribers starting in 1984, the Continent fell behind in the cyberspace race. But now, with 10 million home PCs installed and sales growing rapidly, the market is ripe. CompuServe Inc., the pioneering U.S. online

service, planted its flag in Munich and in Bristol, England, four years ago and now boasts 206,000 subscribers. In 1995, a half-dozen new services will follow, including Europe Online, a Luxembourg-based service backed by British, French, and German publishers.

FORMIDABLE. Overall, market researchers forecast that as many as 500,000 Europeans could go online this year; by 2000, the market could swell to as many as 15 million. Modem sales in Europe grew 39% last year and are expected to jump 35% this year, according to Dataquest Inc., and by 1998 some 17 million modems will be in use on PCs. Even politicians are getting with it: German Foreign Minister Klaus Kinkel got wired on Jan. 14. At the Foreign Ministry's 125th anniversary, Kinkel bantered online with citizens—the first minister's electronic chat in Europe.

While analysts say Europe can sup-

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Information Processing

port three or four services, a showdown is looming between the Americans—CompuServe, America Online, Apple's eWorld, and Microsoft—and homegrown nets such as Europe Online, backed by Germany's Burda, Britain's Pearson, and France's Matra-Hachette.

As in the U.S., the entry by software giant Microsoft Corp. is seen as the key event. The company plans to bundle software to log on to the new Microsoft Network with every copy of its next operating system, Windows 95, now due out in August. Microsoft, which plans to operate its network internationally from the get-go, will gain millions of potential customers overnight—without having to engage in costly marketing programs, which, says Europe Online Chief Executive Christian Bruck, eat up some 30% of operating costs for other networks. "Microsoft will be our most formidable competitor," he says.

But if content is the key to winning market share, Europe Online is likely to have a strong home-court advantage. Its three main shareholders own roughly 500 publications, including the *Financial Times*, Germany's *Focus*, and France's *Elle*. Europe Online's owners are keen on spinning their print empires into electronic gold. By contrast, Microsoft, Apple Computer Inc., and others will have to start mainly with their U.S.-based content and scramble for local European offerings. That's a cause for worry among some U.S. executives: "Do you really think Europeans will buy an American service?" one doubting Microsoft manager asked a reporter at Milia, a January multimedia convention in Cannes where Europe Online made its debut.

VOCAL LOCALS. A big challenge for the Americans will be to come up with services that are geared to each market and language. CompuServe has a handful of local services, including a German newswire and a British "Good Pub Guide." But CompuServe in Europe is mainly aimed at consumers doing research or seeking technical support. "The main strategy is to add local content," says Paulette White, CompuServe's vice-president for international operations.

America Online, now vying with

CompuServe for the lead in the had tried to join the Europe Online sortium. Instead, the consortium decided to license the Interchange technology developed by Ziff Communications and now owned by AT&T. While AOL tools its international plans, it is viding access to the U.S. system in cities in 42 countries. Prodigy has presence beyond North America, is said to be discussing partnerships several major European companies.

In the meantime, Europe Online plans to start up with hundreds of services in French, English, and man by yearend. Europe Online to incorporate an automatic trans

Putting The Old World Online

SERVICE

COMPUSERVE

APPLE eWORLD

EUROPE ONLINE

MICROSOFT NETWORK

DESCRIPTION

The granddaddy of online services has 206,000 members in France, Germany, and England.

Launched in Britain and the U.S. last October, is slated to expand to other parts of the Continent by yearend.

Sponsored by a consortium of European banks and publishers, the service is scheduled to go up in France, Germany and England in 1995.

The software giant's online debut won't happen until Windows 95 is ready, but Microsoft will be international from day one.

DATA: BUSINESS WEEK

program that will allow members of different nationalities to converse each other—a technology that CompuServe is now testing. Another is Italia Online. Backed by computer Olivetti and Milan's top financial newspaper, *Il Sole 24 Ore*, the Italian service will feature local news, interactive logs, and chat networks.

Lagging behind but not out of the race yet, France Telecom also plans to upgrade its ancient but popular Minitel service. Minitel has 6.5 million dedicated terminals and 20,000 service providers. But its slow text-based menu has no match for slick new technologies: the service may soon be forced to consider switching to a PC-based network. But despite its outdated look, Minitel has created popular local services that consumers are buying. And that may be the most valuable lesson of all.

By Gail Edmondson in Cologne

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BOND FUNDS: NOWHERE TO GO BUT UP?

Widespread losses made 1994 abysmal, but the outlook is improving

For the bond market, 1994 will go down in infamy. The debacle was the worst in 60 years. Investors who thought they were being prudent by buying bond funds discovered to their horror that even the highest-quality portfolio lost value in the face of rising rates. After pouring \$113.6 billion into bond funds in 1993, investors did an about-face. They took \$43.5 billion more out of the funds than they put in.

But the case for buying bond funds now seems persuasive. The Federal Reserve, which engineered the rise in interest rates to head off inflation, appears have done the job—and the end of rate hikes is at hand. Funds with short-to-medium maturities look especially attractive. For a five-year bond to lose money over the next year, interest rates would have to top 10%, says Robert L. Rodriguez, portfolio manager of the FPA New Income Fund. "There are some good values in the bond market today," says Rodriguez. Adds Ian A. MacKinnon, the bond-fund chief at the Vanguard Group: "It's time to start buying again."

But which funds? Why not the best? We identify them in BUSINESS WEEK's Mutual Fund Scoreboard. We now report on 652 bond funds, nearly 100 more than last year. We examine how they performed not only in 1994 but during the last three- and five-year periods as well.

For funds with at least five years' history, we assign ratings based on their risk-adjusted returns during the 1990-94 period. Thirty-eight funds, both taxable and tax-free, earned three upward-pointing arrows, the highest BW rating (table). The data in the Scoreboard are

prepared for BUSINESS WEEK by Morningstar Inc.

These top-rated funds performed actively well in 1994's bear market course, in absolute terms, the returns were poor. The average three upward-pointing arrow fund lost money, with a -0.4% total

turn (appreciation reinvestment of dividends and capital gains). Only 16 posted a positive return. The fund was the Strong Advantage Fund, up the worst of the Fidelity Aggressive Free Portfolio, had a -5.9% return. Both have been on the honors list for several years, and in fact, this year's 38 highest rated funds are overs from last year's average return from prior top-honors list covering the 1989-94 period—was -2.5%.

CASUALTIES. If the performance of the top funds is disappointing, consider that the average bond fund in the Scoreboard delivered a sickening -4.9%. It's funds that invest in adjustable-rate mortgages which are supposed to protect investors' principal when interest rates are rising, in the failed to do the job, though a few did rise on the occasion. One fund, Smith Brex Short Duration Government Fund, had the best results of the Scoreboard fund, up 4.3% for the year. 5% of the Scoreboard funds even finished the black for 1994.

THE TOP PERFORMERS

These 38 bond mutual funds have earned three upward-pointing arrows in the BUSINESS WEEK Mutual Fund Scoreboard. To get this rating, they needed to deliver superior risk-adjusted total returns over the last five years.

FUND	AVERAGE ANNUAL TOTAL RETURN*	OBJECTIVE
AIM LIMITED MATURITY TREASURY RETAIL	6.0%	Government-Treasury
AMERICAN CAPITAL TAX-EXEMPT H/Y MUNI. A	7.1	Municipal-national
ASSET MANAGEMENT SHORT U.S. GOVT.	6.7	Government-general
BERNSTEIN GOVT. SHORT DURATION	6.0	Government-general
BERNSTEIN SHORT DURATION PLUS	6.4	Corporate-high-quality
CALVERT TAX-FREE RES. LIMITED-TERM A	4.9	Municipal-national
DREYFUS SHORT-INTERM. GOVERNMENT	7.3	Government-general
DREYFUS SHORT-INTERM. MUNICIPAL BOND	5.5	Municipal-national
DUPREE KENTUCKY TAX-FREE INCOME	7.3	Municipal-single-state
FIDELITY ADVISOR HIGH-YIELD A	15.9	Corporate-high-yield
FIDELITY AGGRESSIVE TAX-FREE	7.0	Municipal-national
FIDELITY CAPITAL & INCOME	13.5	Corporate-high-yield
FIDELITY MORTGAGE SECURITIES	7.4	Government-mortgage
FIDELITY SPARTAN LIMITED MATURITY GOVT.	6.4	Government-general
FIDELITY SPARTAN SHORT-INTERM. MUNI.	5.7	Municipal-national
FLAGSHIP LIMITED-TERM TAX-EXEMPT A	6.4	Municipal-national
FPA NEW INCOME	9.8	Corporate-general
FRANKLIN HIGH-YIELD T/F INCOME	7.3	Municipal-national
INVESCO SELECT INCOME	8.6	Corporate-general
MAINSTAY HI-YIELD CORP. BOND B	12.9	Corporate-high-yield
OPPENHEIMER CHAMPION HI-YIELD A	13.5	Corporate-high-yield
OPPENHEIMER HIGH-YIELD A	10.8	Corporate-high-yield
PORTICO SHORT-TERM BOND RETAIL	7.0	Corporate-general
T. ROWE PRICE TAX-FREE HIGH-YIELD	7.2	Municipal-national
T. ROWE PRICE TAX-FREE SHORT-INTRM.	5.3	Municipal-national
SCUDDER MEDIUM-TERM TAX-FREE	6.8	Municipal-national
SIT TAX-FREE INCOME	6.7	Municipal-national
STRONG ADVANTAGE	7.4	Corporate-general
STRONG GOVERNMENT SECURITIES	8.6	Government-general
THORNBURG LIMITED-TERM MUNI. CA. A	5.5	Municipal-California
THORNBURG LIMITED-TERM MUNI. NATL. A	6.0	Municipal-national
UNITED MUNICIPAL HIGH-INCOME	7.7	Municipal-national
USAA TAX-EXEMPT SHORT-TERM	5.1	Municipal-national
VANGUARD FIXED-INC. S/T CORPORATE	7.2	Corporate-high-quality
VANGUARD MUNICIPAL BOND INTERM.-TERM	7.4	Municipal-national
VANGUARD MUNICIPAL BOND LIMITED-TERM	5.8	Municipal-national
VANGUARD MUNICIPAL BOND SHORT-TERM	4.8	Municipal-national
VENTURE MUNI (+) PLUS B	6.6	Municipal-national

*Pretax, includes reinvestment of dividends and capital gains, 1990-94 DATA: MORNINGSTAR INC.

though derivatives grabbed the headlines last year, the worst derivative-related damage was confined to a handful of funds. The two funds hit the hardest by derivatives are institutional funds not covered in the Scoreboard. Individual investors' fund, Paine-Warner Short-Term U.S. Government Income Fund, had a -4.3% return. It would have been worse if Paine-Warner Inc. had not taken some of the derivatives off the fund's hands. Derivatives claimed some real casualties among the tax-free funds. The New York Muni Fund posted the worst performance of the year, down 20.4%. That's because as interest rates began to rise in early 1994, the fund had nearly half its assets in inverse floaters—and the price of those securities plunged faster than those of conventional bonds. California funds performed poorly, too, not so much because of their own derivatives, but because of Orange County's. The county was thrown into bankruptcy because of investment losses created by derivatives and excessive leverage. And bonds of Orange County issuers slumped in price.

PURCHASES. Of course, derivatives are not all bad. The question is how a fund uses them. For instance, Vanguard's Grant, portfolio manager of the Vanguard Mortgage Securities Fund, invested 2% of the fund's assets into intermediary mortgage securities in late 1993, as prices were bottoming out. "They were very cheap," recalls Grant. "When rates were low, nobody wants them." But as rates rose, so did the value of those securities. Higher rates mean fewer homeowners would refinance mortgages, and mortgage payments would last for a long time. Grant says they added 2 percentage points of return, the difference between a profit and a loss for the year. Among the year's worst performers were world bond funds, with a -8.2% average return. Those with large holdings in emerging markets were in the red before the Mexican currency crisis. The North American Government Income Fund, stuck with hefty holdings in debt when the crisis hit, had a return of -30.8% even considering a 14.3% yield. Ironically, until the end of the quarter, that fund was one of the leading bond funds of the year, according to Financial Research Corp. Investing bond funds for yield alone is a dicey bet. So if you're thinking about investing in bond funds, start your shopping among the funds with three up-

THE YEAR OF RED INK

No category of funds escaped the scourge of rising interest rates. Tax-free funds fared worse than most taxables. World bond funds did worst of all.

FUND OBJECTIVE	TOTAL RETURN*			BEST PERFORMER OF GROUP (1994)
	1994	1992-94**	1990-94**	
GOVT.-ADJ. RATE MTGE.	-2.3%	2.1%	5.2%	Smith Breeden Sh. Dur. U.S. Govt.
GOVT.-MORTGAGE	-2.5	3.4	6.8	Fidelity Mortgage Securities
CORP.-HIGH-QUALITY	-2.7	4.2	7.0	Seven Seas Yield Plus
CONVERTIBLE	-3.5	8.8	9.6	MainStay Convertible B
GOVT.-GENERAL	-3.8	3.4	6.5	Bernstein Govt. Short Duration
CORP.-HIGH-YIELD	-3.8	10.9	10.9	Fidelity Spartan High-Income
CORP.-GENERAL	-4.1	5.1	7.5	Strong Advantage
GOVT.-TREASURY	-4.7	4.1	6.8	Permanent Port. Treasury Bill
MUNI.-NATIONAL	-5.1	4.7	6.3	Calvert Tax-Free Res. Lim.-Term A
MUNI.-SINGLE STATE	-5.8	4.8	6.5	Thornburg NM Intermediate Muni A
SH.-TRM. WORLD INCOME	-6.1	1.0	NA	Dean Witter Global Sh.-Term Income
MUNI.-CALIFORNIA	-6.7	4.4	6.1	Benham CA Tax-Free Short-Term
MUNI.-NEW YORK	-6.9	4.6	6.4	Limited Term NY Municipal
WORLD BOND	-8.2	3.5	7.5	Benham European Government
ALL BOND FUNDS	-4.9	4.8	7.0	
TAXABLE FUNDS	-4.0	5.0	7.7	
TAX-FREE FUNDS	-5.8	4.7	6.4	

*Pretax, includes reinvestment of dividends and capital gains

**Average annual

DATA: MORNINGSTAR INC.

arrow ratings. They've earned these not because they paid out the most money, but because they earned the highest returns for the amount of risk they took.

The list is dominated by funds that keep their portfolios in the short-to-intermediate maturities. True, long-term funds often have the highest yields, and when interest rates fall their value jumps. But over the long haul, the long-term funds don't necessarily return a whole lot more. For instance, Vanguard Fixed-Income Short-Term Corporate Bond Fund, a three-up-arrow fund, delivered a 7.2% average annual total return for the last five years vs. 8.9% a year for the Vanguard Fixed-Income Long-Term Corporate Bond Fund. Yet the short-term fund is the better investment. That's because it has 80% of the return of the long-term fund with about one-third the risk (box, page 96).

That's a point often lost on yield-hungry investors. Long-term bonds can be as volatile as equities, but they don't have nearly the same payoff potential. "If you really want to earn money, go to equity funds," says investment adviser Tim C. Medley, of Medley & Co. in Jackson, Miss. "For bonds, stick to the short term."

If stretching for yield by taking on interest-rate risk does not pay, the top-performers list suggests that taking on some credit risk does. Four of the top funds are high-yield corporate funds, or "junk bond" funds. These earn higher returns by taking on the risk that the issuers can make good on their debts. Such funds can also balance an investment-grade portfolio. When rates rise, junk bonds tend to fall less than high-grades. That's because a strengthening economy that raises rates also boosts corporate cash flows—and the credit-worthiness of lower-rated borrowers.

RARE BIRD. High-yield muni-bond funds have often shown a positive mix of risk and reward, because they earn higher yields by investing in unrated bonds. Many smaller issuers find it cheaper to pay a higher rate on their bonds than shell out for a credit agency's rating. So for fund managers who can perform the credit analysis themselves, like American Capital Tax-Exempt High-Yield Municipal A, unrated bonds can be golden. But high-yield muni funds pick up some of their extra yield by taking on longer-maturity securities. So their 1994 returns suffered more from rising rates than did high-yield corporates.

The case for bond funds now seems persuasive—and those with short-to-medium maturities look especially good

Nearly all individual investors would net more money choosing municipal over tax-free bond funds

One of the more unusual funds on the top-honors list is FPA New Income Fund, a taxable-bond fund with an average annual total return of 9.8% over the last five years and a 1.5% return in 1994. Unlike most bond funds, which are segmented by market (such as government or high-yield) or maturity (short, intermediate, or long-term portfolios), portfolio manager Rodriguez has wide latitude: The portfolio's average maturity can be as short as two years or as long as 10. As interest rates hit record lows in 1993, Rodriguez refused to buy bonds and took the portfolio down to its minimum maturity. That kept him in good stead when the market plunged. Since midyear, he has been

slowly lengthening the maturity of the fund by adding 15-year zero-coupon bonds and 10-year U.S. Treasury notes.

Before you invest, consider your tax status. Tax-exempt funds were even harder hit last year than taxables, and yields on munis are more than 80% of those on taxables of comparable maturity and credit quality. That means nearly all investors—anyone in a 28% or higher tax bracket—could earn a higher yield in muni funds. For tax-deferred accounts, taxables are the way to go.

What's also critical are sales charges and expenses. For instance, FPA New Income is a fine fund, but it has an upfront 4.75% load. That may dissuade some investors. But an upfront load is a

one-time charge. More troublesome are high expense ratios—money that goes out of the fund every year to pay for management, operations, and for the fund's 12(b)-1 fees, a salesperson. Why it may be wise to pass on Vanguard Muni (+) Plus B, despite its three-star rating. It has a steep 2.08% expense ratio—\$2.08 for every \$100 in fund. By comparison, the expense ratio for the average tax-free fund is 1.0% and the average taxable fund, 1.0%.

Such details may sometimes count more than performance. You'll find more data you need in the Scoreboard begins on page 97.

By Jeffrey M. Laderman
in New York

A HELPFUL YARDSTICK FOR ANXIOUS INVESTORS

Investors know that risk in the bond market is directly related to maturity of the bonds. If rates go up, a 30-year bond is going to fall further than a three-year bond. That's because the 30-year bond will be paying a lower-than-market interest rate for a very long time, while the holder of the three-year bond will only have to suffer for a few more years.

But maturity doesn't tell the whole story. Bonds with the same maturity but different coupons can behave much differently in a changing-rate environment. For instance, a 10-year bond with an 8% coupon will be less risky than a 10-year bond with a 6% coupon. Why? Because with a higher coupon, more money comes back to the investor sooner. And the faster your money comes back, the less the risk for holding that bond.

DANGER LOOMING? Bond-fund managers calculate that risk and call it "duration." The duration number tells how much the bond will change in price in response to changes in interest rates. The lower the duration, the less risky the bond. A bond fund's duration is the weighted average duration

of the bonds that are in the fund.

Look at Vanguard's corporate-bond funds in the accompanying table. The duration of the short-term fund is 2.3 years. Compare that with the long-term bond fund, which has a 7.5-year duration. If interest rates go up 1 percentage point, the short-term fund will fall 2.3% in market value while the long-term fund will fall

the risk of the long-term fund.

The biggest problem with bond fund duration is obtaining the data. They are not available in newspaper or most mutual-fund reports. Morningstar Inc., which supplied the data for BUSINESS WEEK's Scoreboard, found that duration figures provided by funds were inaccurate, unavailable, or calculated in ways that made fund-to-fund analysis unreliable. So Morningstar is now crunching its own numbers by calculating duration for every bond in a fund's portfolio—a cumbersome and still-imperfect process. And it's done only for a fraction of all bond funds.

The best place to obtain information on bond-fund duration is from the management company—if it provides any. A Vanguard representative was able to report the duration over its 800 telephone number. "Few people ask for the duration," reports Ian A. MacKinnon, who heads that company's bond funds. "I wish more people would use it." Considering everything that happened during 1994, perhaps they will.

By Jeffrey M. Laderman
in New York

MATURITY VS. DURATION

Getting a Better Understanding of Risk

FUND	MATURITY YEARS	DURATION YEARS
VANGUARD F/I SHORT-TERM CORP. BOND	2.6	2.3
VANGUARD F/I INTERMEDIATE CORP. BOND	8.4	5.6
VANGUARD F/I LONG-TERM CORP. BOND	20.4	7.5

DATA: VANGUARD GROUP OF INVESTMENT COS.

7.5%. (If rates go down 1 percentage point, the long-term fund will rise 7.5% and the others will have proportionate gains.)

You can also use duration to measure relative risk among bond funds. Divide the duration of the long-term fund by that of the short-term fund. The long-term fund's duration is 3.3 times greater than the short-term's—and it's 3.3 times more risky. Or looking at it another way, the short-term fund has about one-third

Bond Funds

MUTUAL FUND SCOREBOARD

To Use The Tables

52 WEEK RATING

These measures risk-adjusted performance. This shows how a fund performed relative to its peers and relative to the risk it took. Risk-adjusted performance is determined by comparing a fund's risk-of-loss (see below) from its historical return. Performance ratings are based on the performance period between 1990, and Dec. 31. For rating purposes, funds are divided into two groups: all bond funds and all funds. Ratings are based on normal statistical distribution in each group and are as follows:

- ▶ SUPERIOR
- VERY GOOD
- GOOD
- AVERAGE
- BELOW AVERAGE
- POOR
- ▶ VERY POOR

RISK

The risk-of-loss factor is the potential for losing money in a fund, calculated as follows: The monthly Treasury bill return is subtracted from the fund's total return for each of the 60 months in the rating period. When a fund has not performed as well as Treasury bills, the result is negative. The sum of these negative numbers is then divided by the number of months in the period. The result is a negative number, and the greater its magnitude, the higher a shareholder's risk of loss.

PERFORMANCE COMPARISON

The tables provide performance data over three time periods. Here are equivalent total returns for the Lehman Brothers bond indexes during those periods:

	GOVT./CORP.	MUNI.
1994	-3.5%	-5.6%
3-year average (1992-94)	4.9%	4.9%
5-year average (1990-94)	7.7%	6.8%

FUND CATEGORIES

Corporate, Government, Municipal,

International, and Convertible.

SALES CHARGE

The cost of buying a fund, commonly called the "load." Many funds take loads out of initial investments, and for ratings purposes, performance is reduced by these charges. Loads on withdrawals can take two forms. Deferred charges decrease over time. Redemption fees are imposed whenever investors sell shares. Funds with none of these charges are called "no-load."

EXPENSE RATIO

Fund expenses for 1994 as a percentage of average net assets. The measures show how much shareholders pay for fund management. Footnotes indicate 12(b)-1 plans, which allocate shareholder money for marketing costs. The average expense ratio is 1.06% for taxable funds, 0.82% for tax-free funds.

TOTAL RETURN

A fund's net gain to investors,

including reinvestment of dividends and capital gains at month-end prices.

YIELD

Income distributions during 1994 expressed as a percent of net asset value, adjusted for capital gains.

MATURITY

The average maturity of the securities in a fund's portfolio, weighted by market value.

TREND

A fund's relative performance during the five 12-month periods from Jan. 1, 1990, to Dec. 31, 1994. The boxes read from left to right, and the level of green in each box tells how the fund performed relative to other funds during the period: for the top quartile; for the second quartile; for the third quartile; and for the bottom quartile. An empty box indicates that a fund is not rated for that time period.

TELEPHONE NUMBERS

See index on page 110.

	RATING	SIZE ASSETS \$MIL	% CHG 1993-94	FEES		PERFORMANCE			PORTFOLIO		TREND 5-YEAR ANALYSIS
				SALES CHARGE (%)	EXPENSE RATIO (%)	TOTAL RETURN (%)			YIELD (%)	MATURITY (YEARS)	
						1 YR	3 YR	5 YR			
CORPORATE											
HIGH-QUALITY BOND	AVG	529.1	-15	No Load	0.95	-4.5	4.0	6.9	5.8	11.4	
INTERMEDIATE HIGH-YIELD BOND	▲	136.3	9	4.00**	1.35†	-2.2	14.1	13.2	10.0	10.1	
HIGH-YIELD A	▲▲	575.6	5	4.75	1.05†	-1.7	11.4	12.3	10.8	8.2	
INCOME A	▲▲▲	200.6	-17	4.75	1.00†	-7.6	4.6	7.0	8.3	9.9	
INCOME BOND CORPORATE BOND A	▲▲▲	212.9	-15	4.25	1.30†	-12.7	9.0	10.0	9.6	16.4	
CAN CAPITAL CORP BOND A	AVG	161.0	-13	4.75	1.09†	-4.3	5.1	7.7	7.6	14.3	
CAN CAPITAL H/Y INVMNT. A	▲	361.7	-19	4.75	1.10†	-3.6	10.5	9.9	10.0	8.1	
CAN HIGH-INCOME	▲	798.2	1	4.75	0.86†	-5.1	8.3	11.0	9.7	6.4	
ON BOND L	▲	139.0	-13	No Load	0.98	-3.3	5.1	7.5	7.3	8.2	
STEIN INTERMEDIATE DURATION	▲	842.3	16	No Load	0.65	-3.2	4.5	7.4	5.6	12.8	
STEIN SHORT DURATION PLUS	▲▲▲	507.1	0	No Load	0.65	0.5	4.0	6.4	4.8	3.0	
ORE FIXED-INCOME	▲	144.5	5	4.50	0.71	-3.8			6.2	13.0	
ORE SHORT-TERM FIXED-INCOME	▲	147.8	-5	4.50	0.63	1.2			4.7	1.9	
HARD FLEXIBLE INCOME	▲	272.1	-61	No Load	1.30†	-5.5			7.1	6.3	
FUND OF AMERICA	AVG	4941.2	-6	4.75	0.71†	-5.0	6.5	8.6	8.3	7.6	
IAL HIGH-YIELD SECURITIES A	▲	389.6	-12	4.75	1.23†	-0.3	13.1	12.1	10.0	7.9	
IAL INCOME A	▲	129.6	-17	4.75	1.11†	-4.1	5.3	7.3	8.3	15.0	
IAL STRATEGIC INCOME A	▲	637.1	-4	4.75	1.21†	-3.7	6.7	7.7	9.1	10.1	
IBIA FIXED-INCOME SECURITIES	▲	252.1	-16	No Load	0.66	-3.4	4.9	7.9	6.8	6.4	
ASS CAPITAL FIXED-INCOME	AVG	236.9	-14	3.75	0.86	-3.8	4.8	7.3	6.1	10.5	
ASS CAPITAL SHORT/INTERMED.	▲	202.9	-25	3.75	0.85	-0.5	4.3	6.6	5.3	3.6	
WITTER HIGH-YIELD SECS.	▲▲▲	432.2	-22	5.50†	0.69	-7.1	14.9	8.7	12.6	8.3	
WITTER INTERMEDIATE INCOME	▲	224.6	-14	5.00**	1.63†	-3.1	3.8	5.9	6.1	NA	
ARE DELCHESTER A	AVG	948.1	-6	4.75	1.05†	-4.6	9.2	10.4	12.1	6.9	
VERNMENT INCOME	▲	177.3	75	2.00	0.71†	-3.4			5.7	9.5	
E & COX INCOME	▲	195.4	9	No Load	0.53	-2.9	5.2	8.1	7.0	12.2	
US A BONDS PLUS	▲	485.7	-23	No Load	1.00	-6.2	5.3	7.8	7.1	15.7	
US SHORT-TERM INCOME	▲	222.5	-31	No Load	0.24†	0.1			7.2	2.7	
US STRATEGIC INCOME	AVG	309.3	-20	3.00	0.84†	-6.3	5.5	8.1	7.3	11.9	
RATHON HIGH-INCOME (a)	▲▲	414.7	-1	5.00**	1.77†	-1.8	10.6	8.8	10.4	7.4	

† is redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts. NA = Not available. NM = Not meaningful. (a) Formerly Eaton High-Income. DATA: MORNINGSTAR INC., CHICAGO, IL

MUTUAL FUND SCOREBOARD

Bond Fu

	RATING	SIZE ASSETS \$MIL	% CHG 1993-94	FEES		PERFORMANCE			PORTFOLIO		TR 5- ANA
				SALES CHARGE (%)	EXPENSE RATIO (%)	TOTAL RETURN (%)			YIELD (%)	MATURITY (YEARS)	
						1 YR	3 YR	5 YR			
FIDELITY ADVISOR HIGH-YIELD A	◆◆◆	682.8	24	4.75	1.22†	-2.1	13.0	15.9	7.0	6.0	
FIDELITY ADVISOR LIM-TERM BOND A	◆◆◆	146.5	114	4.75	1.18†	-2.5			5.9	5.3	
FIDELITY ADVISOR SHORT FIXED-INC. A	◆◆◆	690.7	-9	1.50	0.97†	-3.4	4.4	6.5	6.3	2.5	
FIDELITY CAPITAL & INCOME	◆◆◆	2039.8	-26	1.50*	0.95	-5.1	14.7	13.5	8.7	6.6	
FIDELITY INTERMEDIATE BOND	◆◆◆	2127.4	16	No Load	0.62	-2.0	5.2	7.5	6.5	6.5	
FIDELITY INVESTMENT GRADE BOND	◆◆	995.1	-5	No Load	0.76	-5.4	6.0	8.5	7.2	9.6	
FIDELITY SHORT-TERM BOND	◆◆	1514.8	-39	No Load	0.76	-4.1	4.0	6.3	6.6	2.4	
FIDELITY SPARTAN HIGH-INCOME	◆◆	617.5	-7	1.00*	0.80	2.6	14.7		8.1	5.3	
FIDELITY SPARTAN INVMT. GRADE BD.	◆◆	118.0	-2	No Load	0.65	-4.6			8.1	17.4	
FIDELITY SPARTAN S/T INCOME	◆◆	610.3	-59	No Load	0.54	-4.6			6.8	3.0	
FIRST INVESTORS FUND FOR INCOME A	◆◆	399.0	-7	6.25	1.26†	-0.2	11.2	10.3	9.2	7.6	
FIRST INVESTORS HIGH-YIELD A	◆◆	169.4	-11	6.25	1.61†	-0.4	11.5	9.2	9.1	6.5	
FORTRESS BOND	AVG	142.3	0	2.00*	1.05†	-3.4	9.2	11.2	8.3	8.2	
FPA NEW INCOME	◆◆◆	129.9	13	4.50	0.74	1.5	7.5	9.8	6.7	4.8	
FRANKLIN AGE HIGH-INCOME	AVG	1719.6	-34	4.25	0.59†	-1.5	10.5	11.4	10.2	8.7	
HANCOCK HIGH-YIELD BOND B (b)	AVG	153.0	-1	5.00**	2.08†	-6.1	8.9	10.1	10.4	7.6	
HANCOCK SOVEREIGN BOND A	AVG	1321.8	-12	4.50	1.25†	-2.8	5.3	7.8	8.0	11.5	
HANCOCK STRATEGIC INCOME A	◆◆	317.9	-6	4.50	1.32†	-3.1	5.8	7.4	9.5	8.1	
HARBOR BOND	◆◆	167.0	-3	No Load	0.77	-3.8	5.7	8.8	5.9	7.6	
IDS BOND	AVG	2135.5	-14	5.00	0.68	-4.3	6.9	9.1	8.3	13.7	
IDS EXTRA INCOME	◆◆	1526.0	-8	5.00	0.79	-7.6	9.8	10.4	11.6	8.2	
IDS SELECTIVE	AVG	1392.9	-19	5.00	0.71	-4.4	5.6	8.0	6.9	14.0	
IDS STRATEGY INCOME	◆◆	643.2	-17	5.00**	1.64†	-7.8	5.3	7.5	5.3	13.2	
IDS STRATEGY SHORT-TERM INCOME	◆◆	215.3	21	5.00**	1.71†	-2.2	2.3	4.5	2.8	5.7	
INTERMEDIATE BOND FUND AMERICA	AVG	1449.3	-17	4.75	0.83†	-3.0	4.0	6.8	7.3	4.6	
INVESCO HIGH-YIELD	AVG	210.8	-31	No Load	0.97†	-5.0	8.0	8.2	10.2	9.2	
INVESCO SELECT INCOME	◆◆◆	136.7	-13	No Load	1.11†	-1.2	6.7	8.6	7.6	14.1	
IVY BOND A (c)	◆◆	109.7	-16	4.75	1.45	-4.5	5.9	7.0	6.6	10.0	
JANUS FLEXIBLE INCOME	AVG	353.9	-25	No Load	0.93	-2.9	7.9	8.6	8.2	10.0	
KEMPER DIVERSIFIED INCOME A	AVG	460.9	34	4.50	1.12	-3.7	11.1	12.7	9.3	8.0	
KEMPER HIGH-YIELD A	AVG	2249.5	-2	4.50	0.86	-1.7	11.4	12.1	10.1	7.8	
KEMPER INC. & CAPITAL PRESERVATION A	AVG	486.7	-13	4.50	0.83	-3.4	5.2	7.9	7.9	9.8	
KEYSTONE AMER. STRATEGIC INCOME B	◆◆	152.1	31	3.00**	2.07†	-10.3			8.7	8.2	
KEYSTONE CUSTODIAN B-1	◆◆	323.8	-26	4.00**	1.83†	-5.1	2.4	5.6	6.5	9.7	
KEYSTONE CUSTODIAN B-2	◆◆	736.0	-27	4.00**	1.75†	-6.9	5.2	6.2	7.8	11.4	
KEYSTONE CUSTODIAN B-4	◆◆◆	669.4	-34	4.00**	1.84†	-12.2	9.4	7.7	10.0	7.7	
LIBERTY HIGH-INCOME BOND A	◆◆	421.2	-9	4.50	1.20	-1.7	10.6	13.6	10.0	7.6	
LIMITED TERM A (d)	◆◆	170.2	-30	1.00	1.10†	-1.3	4.0		5.8	2.7	
LORD ABBETT BOND-DEBENTURE	AVG	987.6	2	4.75	0.88†	-3.9	9.0	10.6	10.1	8.0	
MAINSTAY HI-YIELD CORP. BOND B	◆◆◆	1122.1	20	5.00**	1.60†	1.5	14.5	12.9	9.0	7.0	
MARSHALL INTERMEDIATE BOND	◆◆	326.1	4	No Load	0.71	-3.1			6.5	3.9	
MERRILL LYNCH CORP. HIGH-INCOME B	◆◆	2249.1	9	4.00**	1.28†	-4.7	10.0	11.8	8.8	8.3	
MERRILL LYNCH CORP. INTERM-TERM A	◆◆	157.4	-16	1.00	0.52	-4.7	4.4	7.3	6.9	6.0	
MERRILL LYNCH CORP. INVMT. GR. B (e)	◆◆	471.9	-7	4.00**	1.27†	-6.0	2.6	5.9	6.2	9.9	
MERRILL LYNCH WORLD INCOME B	◆◆	1490.5	-29	4.00**	1.52†	-5.1	3.9		7.7	NA	
METLIFE-STATE ST. RES. HIGH-INC. A (f)	◆◆	591.3	-6	4.50	1.23†	-2.8	12.7	10.3	10.5	6.5	
MFS BOND A	AVG	434.6	-12	4.75	0.96†	-4.5	5.0	7.9	7.4	11.8	
MFS HIGH-INCOME A	◆◆	501.7	-20	4.75	0.98†	-2.6	10.8	11.0	9.2	8.3	
MFS INTERMEDIATE INCOME B	◆◆	285.7	-39	4.00**	2.22†	-6.4	1.5	4.6	4.2	4.7	
NATIONWIDE BOND	◆◆	121.6	-20	4.50	0.71	-7.9	3.2	6.8	8.0	12.9	
NEUBERGER & BERMAN LTD. MAT.	◆◆	293.9	-15	No Load	0.67	-0.3	3.8	6.4	5.8	2.2	
NEW ENGLAND BOND INCOME A (g)	AVG	155.8	-13	4.50	1.08†	-4.2	4.8	7.9	6.6	9.0	
NICHOLAS INCOME	◆◆	140.9	-11	No Load	0.59	-0.2	7.5	8.7	9.4	7.0	
NORTHEAST INVESTORS	◆◆	554.6	1	No Load	1.06	2.2	14.1	11.2	10.3	7.1	
OPPENHEIMER CHAMPION HI-YIELD A	◆◆◆	174.9	42	4.75	1.22†	-0.1	12.1	13.5	8.6	7.1	
OPPENHEIMER HIGH-YIELD A	◆◆◆	958.3	-17	4.75	0.96†	-2.3	10.3	10.8	10.5	9.4	
OPPENHEIMER STRATEGIC INCOME A	◆◆	2986.9	-1	4.75	0.99†	-4.7	7.1	9.9	9.2	NA	
PAINEWEBBER HIGH-INCOME A	AVG	256.6	-42	4.00	0.90†	-11.7	10.4	12.6	12.3	7.3	
PAINEWEBBER INVMT. GRADE INCOME A	AVG	265.0	29	4.00	1.09†	-5.6	5.2	8.0	7.9	13.2	
PARAGON INTERMEDIATE-TERM BOND	◆◆	293.8	-14	4.50	0.77	-4.6	3.6	6.7	6.8	7.2	
PARAGON SHORT-TERM GOVERNMENT	◆◆	139.6	-18	4.50	0.77	0.0	3.7	6.1	5.1	2.2	
PHOENIX HIGH-YIELD A	AVG	504.2	-29	4.75	1.19†	-8.0	9.3	10.0	10.1	7.9	
PHOENIX MULTI-SECTOR FIXED-INC. A	◆◆	162.5	-30	4.75	1.06†	-6.8	6.4	10.2	8.2	9.8	
PIERPONT BOND	AVG	110.8	5	No Load	0.79	-4.0	2.7	6.3	4.8	9.4	
PIMCO ADV HIGH-INCOME C (h)	◆◆◆	148.5	-38	1.00**	1.90†	-7.1	2.2	4.1	7.9	7.5	
PORTICO BOND IMMDEX RET.	◆◆	249.5	-2	2.00	0.49	-3.1	5.0	7.9	6.5	6.9	
PORTICO SHORT-TERM BOND RET.	◆◆◆	116.3	-15	2.00	0.50	1.0	4.7	7.0	5.9	2.7	
T. ROWE PRICE HIGH-YIELD	◆◆	1040.4	-36	1.00*	0.88	-8.0	8.7	8.4	9.7	7.2	
T. ROWE PRICE NEW INCOME	◆◆	1367.8	-12	No Load	0.82	-2.2	3.8	7.1	6.8	10.1	
T. ROWE PRICE SHORT-TERM BOND	◆◆	474.9	-30	No Load	0.74	-2.9	2.8	5.6	6.0	2.2	

* Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not a mutual fund.
 (b) Formerly Transamerica Special High-Yield Bd. (c) Formerly Mackenzie Fixed-Income A. (d) Formerly Limited Term Invmt. (e) Formerly Merrill Lynch High Quality B. (f) Formerly M
 State Street High-Income A. (g) Formerly TNE Bond Income A. (h) Formerly Thomson Income A.

DATA: MORNINGSTAR INC., CHICAGO

TOTAL FUND SCOREBOARD

Bond Funds

	RATING	SIZE ASSETS \$MIL.	% CHG. 1993-94	FEES		PERFORMANCE			PORTFOLIO		TREND 5-YEAR ANALYSIS
				SALES CHARGE (%)	EXPENSE RATIO (%)	TOTAL RETURN (%)			YIELD (%)	MATURITY (YEARS)	
						1 YR	3 YR	5 YR			
ENTIAL HIGH-YIELD B	AVG	3327.9	-11	5.00**	1.35†	-3.0	9.4	9.7	10.0	8.4	
ENTIAL STRUCTURED MATURITY B		130.4	6	3.00**	1.56†	-2.0			5.2	3.0	
IM DIVERSIFIED INCOME B		1561.4	60	5.00**	1.76†	-6.2			8.0	8.2	
IM HIGH YIELD A	♦♦♦	2715.0	-17	4.75	0.94†	-4.7	10.4	12.1	11.0	8.7	
IM HIGH YIELD ADVANTAGE A	♦♦♦	666.4	-12	4.75	0.96†	-5.1	10.8	12.8	11.3	8.4	
IM INCOME A	AVG	764.4	-6	4.75	0.79†	-3.3	5.9	8.0	8.0	8.8	
ER INCOME	AVG	464.1	-9	No Load	0.96	-4.5	4.7	7.9	6.2	11.0	
ER SHORT-TERM BOND	♦♦	2138.8	-33	No Load	0.72	-2.9	3.4	6.8	6.9	1.5	
SEAS YIELD PLUS		1209.9	-2	No Load	0.35†	4.1			4.4	0.4	
A CORPORATE INCOME A		361.2	-28	4.50	1.35†	-10.3	4.6		8.7	20.6	
BARNEY DIV. STRAT. INCOME B (i)	♦♦	2247.7	-7	4.50**	1.57†	-3.4	4.9	8.4	8.4	14.7	
BARNEY HIGH-INCOME B (j)	AVG	401.2	-20	4.50**	1.60†	-5.0	10.6	9.6	10.1	6.2	
BARNEY INVMT. GRADE BD. B (k)	♦♦♦	215.3	-54	4.50**	1.58†	-9.3	5.1	7.9	7.6	26.2	
ROE INCOME	♦	152.8	-6	No Load	0.82	-4.1	5.9	8.1	7.5	7.1	
ROE INTERMEDIATE BOND	♦	281.5	-14	No Load	0.70	-2.8	4.6	7.1	6.7	6.2	
IG ADVANTAGE	♦♦♦	910.5	119	No Load	0.80	3.6	6.7	7.4	5.5	0.5	
IG INCOME	♦	123.3	0	No Load	1.10	-1.3	8.0	6.3	7.9	11.6	
IG SHORT-TERM BOND	♦♦	1041.1	-32	No Load	0.90	-1.8	4.6	6.7	6.7	2.5	
ERICA DIVERSIFIED INCOME B		155.7	19	4.00**	2.06†	-8.9	1.0		9.3	7.9	
ERICA HIGH-INCOME B		108.6	-29	4.00**	2.31†	-9.4			11.9	7.6	
FIETH CENTURY LONG-TERM BOND	♦	119.8	-24	No Load	0.88	-4.5	3.6	6.7	6.7	9.8	
D BOND	♦♦	518.0	-19	5.75	0.73†	-5.8	4.7	7.3	6.9	8.3	
D HIGH-INCOME	♦♦	908.0	-14	5.75	0.83†	-3.7	9.8	9.1	9.3	8.4	
D HIGH-INCOME II	♦	343.9	-13	5.75	0.88†	-4.1	9.2	10.1	9.2	7.7	
AMPEN HIGH-YIELD A	♦	238.2	-9	4.65	1.32†	-3.6	9.9	9.7	11.2	6.8	
ARD BOND IDX TOTAL BOND MKT. (l)	♦	1730.7	12	No Load	0.18	-2.7	4.6	7.5	6.8	8.9	
ARD F/I INTERM-TERM CORP BD.		151.5	134	No Load	0.29	-4.2			6.5	7.9	
ARD F/I HIGH-YLD. CORP.	♦	2120.7	-16	1.00*	0.35	-1.7	9.9	10.0	9.4	9.2	
ARD F/I L/T CORP BOND	AVG	2552.3	-19	No Load	0.33	-5.3	6.0	8.9	7.6	20.7	
ARD F/I S/T CORPORATE	♦♦♦	2905.8	-17	No Load	0.29	-0.1	4.7	7.2	5.7	2.4	
RY INTERMEDIATE INCOME (m)		115.7	14	4.75	0.76	-2.4			6.5	4.3	
JRG PINCUS FIXED-INCOME	♦	105.2	25	No Load	0.75	-0.8	5.5	7.1	7.0	6.7	
IM BLAIR INCOME SHARES		143.9	-30	No Load	0.74	-0.7	4.9		6.6	9.4	
WARD BOND RETAIL		424.5	-12	4.50	0.73†	-7.0	3.3		6.7	6.4	
WARD INTERMEDIATE BOND RETAIL		391.1	-7	4.50	0.73†	-6.4	2.5		6.1	4.4	
ERNMENT											
GNMA & U.S. TREASURY	♦♦	5248.9	-21	No Load	0.66	-1.7	3.5	6.9	6.5	4.5	
ITAGE GOVERNMENT SECURITIES	♦	152.6	-17	4.00**	1.30†	-9.8	5.5	7.9	6.6	NA	
VERNMENT SECURITIES A	AVG	157.6	13	4.75	1.02†	-3.4	3.2	6.3	8.0	6.5	
D. MATURITY TREASURY RETAIL	♦♦♦	266.0	-22	1.00	0.47†	0.8	3.6	6.0	4.3	1.5	
NCE BOND U.S. GOVERNMENT B		706.2	-10	3.00**	1.72†	-5.0	3.0		7.9	6.7	
NCE MORTGAGE SEC. INCOME B		921.6	-37	3.00**	1.69†	-6.8			6.6	NA	
NCE MORTGAGE STRATEGY B		135.1	-19	3.00**	1.93†	-0.4			4.8	NA	
CAN CAPITAL GOVT. SEC. A	♦	2580.4	-25	4.75	1.03†	-4.3	3.3	6.9	7.0	6.0	
CAN CAPITAL U.S. GOVT. INC. B		208.4	-24	4.00**	1.82†	-4.9			7.2	NA	
MANAGEMENT ADJ. RATE MTG.		862.9	-39	No Load	0.46†	2.0	3.7		4.8	5.8	
MANAGEMENT INTERM. MTG. SEC.	♦	210.5	-10	No Load	0.37†	-1.8	4.3	7.0	5.9	13.3	
MGMT. SHORT U.S. GOVT. (n)	♦♦♦	165.1	-30	No Load	0.47†	0.2	4.2	6.7	5.4	1.5	
U.S. GOVT. & MORTGAGE SEC. A		245.7	-21	3.00	0.80†	-3.3	3.9		7.4	NA	
ADJUSTABLE RATE INCOME		140.9	-31	3.25	0.50†	-6.6			5.6	NA	
IM ADJUSTABLE RATE GOVT. SEC.		443.3	-59	No Load	0.56	-1.2	2.5		5.0	2.2	
IM GNMA INCOME	♦♦♦	952.3	-24	No Load	0.57	-1.5	4.2	7.6	7.0	8.7	
IM TARGET MATURITIES 2000	♦♦♦	255.0	-11	No Load	0.59	-7.2	4.6	7.7	5.3	5.9	
IM TARGET MATURITIES 2015	♦♦♦	122.7	64	No Load	0.68	-14.2	3.3	4.8	3.0	20.7	
IM TARGET MATURITIES 2020	♦♦♦	121.5	152	No Load	0.70	-17.7	4.0	8.0	1.7	25.4	
IM TREASURY NOTE	♦	296.2	-24	No Load	0.53	-2.3	3.9	6.9	5.2	2.9	
TEIN GOVT. SHORT DURATION	♦♦♦	143.4	-25	No Load	0.68	0.3	3.4	6.0	4.5	1.7	
NAL GOVERNMENT OBLIGATIONS	♦♦	158.1	-20	4.50	0.73	-0.9	3.3	6.5	8.2	10.9	
IAL FEDERAL SECURITIES A	♦♦	1242.8	-24	4.75	1.16†	-5.8	3.9	6.6	7.5	14.0	
IAL U.S. GOVERNMENT B		745.0	-27	5.00**	1.86†	-2.5			5.8	4.6	
DN SENSE GOVERNMENT	♦	326.2	-7	6.75	0.89	-5.1	3.1	6.5	6.3	6.1	
OSITE U.S. GOVERNMENT SEC. A	♦	188.1	-30	4.00	1.00†	-4.9	2.9	6.5	6.5	9.9	
WITTER FEDERAL SECURITIES	♦	809.6	-25	5.00**	1.51†	-5.1	3.3	6.2	7.0	10.0	
WITTER SHORT-TERM U.S. TREAS.		329.3	-53	No Load	0.79†	-1.3	3.0		4.9	NA	
WITTER U.S. GOVT. SECURITIES	AVG	8199.9	-33	5.00**	1.21†	-3.6	3.0	5.7	6.8	8.6	
ARE TREAS. RES. INTERM. A	♦	786.4	-30	3.00	0.88†	-1.9	3.0	6.2	7.4	3.5	
ARE U.S. GOVERNMENT A	♦	208.0	-14	4.75	1.23†	-5.8	2.6	6.2	8.8	7.2	
US 100% U.S. TREASURY INTRM.	♦	184.7	-27	No Load	0.88	-4.0	4.6	7.4	7.5	5.7	
US 100% U.S. TREASURY L/T	♦♦	124.1	-42	No Load	0.95	-9.2	4.4	7.6	7.6	19.0	

is redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful.
 rly Smith Barney Shearson Div. Strat. Inc. B. (j) Formerly Smith Barney Shearson High-Income B. (k) Formerly Smith Barney Shearson Invstm. Gr. Bd. B. (l) Formerly Vanguard Bond
 n) Formerly Society Intermediate Income. (n) Formerly Asset Management Int-Term Liquidity

DATA: MORNINGSTAR INC., CHICAGO, IL

MUTUAL FUND SCOREBOARD

Bond Funds

	RATING	SIZE ASSETS \$ MIL.	% CHG 1993-94	FEES		PERFORMANCE			PORTFOLIO		TREND 5-Y ANAL.
				SALES CHARGE (%)	EXPENSE RATIO (%)	TOTAL RETURN (%)			YIELD (%)	MATURITY (YEARS)	
						1 YR	3 YR	5 YR			
DREYFUS 100% U.S. TREASURY S/T	▲	172.4	-8	No Load	0.29	-0.3	4.5	6.5	7.9	2.8	
DREYFUS GNMA	▲	1427.9	-20	No Load	0.96†	-2.8	3.5	6.8	6.9	9.5	
DREYFUS SHORT-INTERM. GOVERNMENT	▲▲	472.1	-13	No Load	0.42	-0.8	4.5	7.3	7.2	2.2	
EV TRADITIONAL GOVT. OBLIGATIONS	▲	386.4	-23	4.75	1.60†	-2.0	4.1	7.0	8.0	4.8	
FEDERATED U.S. GOVERNMENT BOND	AVG	143.1	38	No Load	0.83	-6.3	4.7	7.3	5.9	16.8	
FIDELITY ADVISOR GOVT. INVNT. A	AVG	123.6	64	4.75	0.74†	-3.8	3.9	6.7	5.9	10.3	
FIDELITY GINNIE MAE	▲▲	704.5	-21	No Load	0.82	-2.0	3.6	6.9	6.3	9.1	
FIDELITY GOVERNMENT SECURITIES	▲	611.2	-19	No Load	0.69	-5.2	4.7	7.9	6.7	10.8	
FIDELITY MORTGAGE SECURITIES	▲▲▲	349.4	-7	No Load	0.79	1.9	4.5	7.4	6.0	8.5	
FIDELITY SHORT-INTERMEDIATE GOVT		151.2	0	No Load	0.95	-1.4	2.9		6.4	3.7	
FIDELITY SPARTAN GINNIE MAE		347.8	-40	No Load	0.65	-1.5	3.5		6.7	9.2	
FIDELITY SPARTAN GOVT. INCOME	AVG	231.9	-38	No Load	0.65	-3.6	3.5	6.8	7.4	10.4	
FIDELITY SPARTAN LTD. MAT. GOVT.	▲▲▲	830.6	-39	No Load	0.65	-1.0	3.7	6.4	5.9	4.7	
FIRST INVESTORS GOVERNMENT A	▼	218.1	-24	6.25	1.42†	-3.8	1.9	5.9	5.9	4.5	
FIRST UNION U.S. GOVT. C INVMT.		195.3	-17	5.00**	1.44†	-3.7			6.7	7.7	
FORTIS U.S. GOVERNMENT SEC. E	▼	489.4	-24	4.50	0.77	-5.6	2.6	6.3	8.2	5.9	
FORTRESS ADJUST RATE U.S. GOVT.		435.8	-48	1.00*	1.02†	-0.3	2.6		4.7	3.6	
FRANKLIN ADJUSTABLE U.S. GOVT. SEC.	AVG	684.0	-52	2.25	0.40†	-1.9	1.1	4.2	3.7	1.6	
FRANKLIN SH-INTRM U.S. GOVT. SEC.	▲	221.0	-18	2.25	0.65†	-2.6	3.8	6.6	4.4	2.1	
FRANKLIN TAX-ADVANT U.S. GOVT.	AVG	456.4	-20	4.25	0.57†	-5.3	3.2	6.8	6.0	11.0	
FRANKLIN U.S. GOVERNMENT	▲	10984.6	-21	4.25	0.55†	-2.7	3.8	7.1	7.8	9.0	
FUND FOR U.S. GOVERNMENT SEC. A	AVG	1358.5	-26	4.50	0.95	-1.9	2.7	6.1	7.5	5.4	
GOVERNMENT INCOME SECURITIES	▲	2559.4	-31	2.00**	0.97†	-1.9	2.9	6.2	7.5	5.4	
GRADISON-MCDONALD GOVT. INCOME	AVG	184.0	-31	2.00	0.89†	-3.7	3.3	6.4	6.2	7.0	
HANCOCK GOVERNMENT INCOME B (o)	▼▼	234.5	-19	5.00**	2.01†	-5.3	2.4	5.7	7.6	5.5	
HANCOCK GOVERNMENT SECURITIES A (p)	▼▼	498.9	-26	4.75	1.16†	-4.0	3.3	7.0	8.2	7.9	
HANCOCK LIMITED-TERM GOVT. A	▲	216.9	-18	3.00	1.40†	-1.3	3.3	6.0	4.5	2.1	
HANCOCK SOVEREIGN U.S. GOVT. A		311.0	-14	4.50	1.23†	-4.1			7.0	12.3	
IDS FEDERAL INCOME	▲▲	1010.5	0	5.00	0.76	-0.3	4.0	6.5	5.7	8.6	
INVESTORS TRUST GOVERNMENT B	▼	1203.0	-13	5.00**	1.76†	-9.3	1.1	5.2	7.9	6.6	
ISI TOTAL RETURN U.S. TREASURY	▼▼	195.0	-12	4.45	0.77†	-4.0	4.5	7.1	7.0	8.9	
KEMPER ADJ RATE U.S. GOVT. A	AVG	158.4	-32	3.50	0.93	-0.4	3.5	6.1	5.0	4.3	
KEMPER SHORT-INTERM. GOVT. B (q)	AVG	226.1	-20	4.00**	1.93†	-1.9	2.6	5.2	5.7	1.7	
KEMPER U.S. GOVERNMENT SEC. A	AVG	4746.0	-27	4.50	0.75	-3.1	2.5	6.7	8.4	5.8	
KEMPER U.S. MORTGAGE A (r)		1854.0	1	4.50	0.99	-3.5			7.6	5.7	
LEGG MASON U.S. GOVT. INT.-TM. PRIM.	▲▲	235.0	-22	No Load	0.90†	-2.2	3.5	6.8	5.0	5.2	
LEXINGTON GNMA INCOME	AVG	132.4	-12	No Load	0.97	-2.1	3.6	7.1	7.2	NA	
LIBERTY FINANCIAL U.S. GOVT.	▲	685.9	-26	4.50	0.99†	-1.6	3.3	6.8	7.2	7.8	
LORD ABBETT U.S. GOVT.	▼	3219.6	-18	4.75	0.89†	-4.3	3.9	7.6	9.5	8.2	
LORD ABBETT U.S. GOVT. SEC. TRUST		326.0	-1	1.00*	NA †	-5.5			8.2	7.6	
MAINSTAY GOVERNMENT B	▼	1020.7	-17	5.00**	1.70†	-2.8	2.2	5.3	7.4	6.5	
MERRILL LYNCH ADJ RATE SEC. B		243.9	-47	4.00**	1.46†	-0.1	1.8		4.1	1.4	
MERRILL LYNCH FEDERAL SEC. B		1288.7	-34	4.00**	1.33†	-4.0	2.5		5.6	6.9	
MFS GOVERNMENT LTD. MATURITY A	AVG	256.2	-26	2.50	0.96†	-0.8	4.2	5.1	6.0	1.6	
MFS GOVERNMENT MORTGAGE B		1067.6	-33	4.00**	1.94†	-2.8			6.8	9.1	
MFS GOVERNMENT SECURITIES A	AVG	313.9	-19	4.75	0.79†	-3.3	4.4	7.0	8.0	6.6	
NEW ENGLAND ADJ. RATE U.S. GOVT. A (s)		491.6	-33	3.00	0.60†	0.8	3.2		4.3	2.5	
NEW ENGLAND GOVERNMENT SEC. A (t)	▼▼▼	148.3	-18	4.50	1.28†	-5.5	3.2	6.0	6.6	7.0	
NEW ENGLAND LTD-TM. U.S. GOVT. A (u)	AVG	413.1	-26	3.00	1.17†	-2.2	3.2	6.7	6.3	4.0	
OPPENHEIMER LIMITED-TERM GOVT. A (v)	▲▲	247.8	40	3.50	0.99†	0.5	4.2	7.6	7.4	NA	
OPPENHEIMER U.S. GOVERNMENT A	AVG	299.4	-18	4.75	1.14†	-1.3	3.9	6.8	7.5	4.8	
OVERLAND EXPRESS VAR. RATE GOVT. A		1215.5	-38	3.00	0.79†	-3.8	1.7		4.7	1.3	
PAINEWEBBER S/T U.S. GOVT. INC. D		263.8	-77	No Load	1.28†	-4.9			4.8	2.9	
PAINEWEBBER U.S. GOVT. INCOME A	▼▼	413.8	-36	4.00	0.91†	-10.5	0.4	5.0	7.2	6.6	
PERMANENT PORT TREASURY BILL	▲▲	122.1	-9	No Load	0.78†	3.3	2.8	4.2	1.0	0.2	
PHOENIX U.S. GOVT. SECURITIES A	AVG	254.8	-23	4.75	0.98†	-3.5	4.0	6.8	6.7	8.0	
PILGRIM ADJUSTABLE RATE SEC. I-A		154.7	-20	4.00**	1.16†	-20.5			7.5	NA	
PILGRIM ADJUSTABLE U.S. GOVT. I		309.5	-51	4.00**†	1.30†	-12.6	-1.5		5.6	2.3	
PIMCO ADV U.S. GOVERNMENT C (w)	▼	311.6	-38	1.00**	1.70†	-5.3	1.3	5.1	6.2	7.2	
PIONEER AMERICA INCOME A (x)	AVG	161.3	53	4.50	1.00†	-4.0	3.8	6.4	7.0	NA	
PREMIER GNMA A	▲	141.9	-28	4.50	0.89†	-2.9	3.8	7.4	6.5	NA	
T. ROWE PRICE ADJ. RATE U.S. GOVT.		120.9	-52	No Load	0.40	-0.6	2.0		5.1	0.7	
T. ROWE PRICE GNMA	▲▲	752.2	-18	No Load	0.76	-1.6	3.6	7.1	7.6	9.0	
T. ROWE PRICE U.S. INTERMEDIATE	▲	163.1	-4	No Load	0.69	-2.2	3.9	7.0	6.1	4.0	
PRINCOR GOVERNMENT SEC. INCOME A	▼	247.3	-3	5.00	0.95†	-4.9	3.3	7.1	6.7	11.4	
PRUDENTIAL GNMA B	AVG	245.6	-23	5.00**	1.66†	-2.7	2.4	5.4	6.3	8.8	
PRUDENTIAL GOVERNMENT INCOME B (y)	▼	1538.3	-34	5.00**	1.65†	-4.8	2.7	5.8	6.3	7.8	
PRUDENTIAL GOVERNMENT INT-TRM. A	▲	223.8	-35	No Load	0.80†	-2.6	3.5	6.3	6.7	3.7	
PUTNAM AMERICAN GOVERNMENT INC. A	▼▼	2244.7	-30	4.75	0.83†	-2.9	3.0	5.1	7.7	10.1	
PUTNAM FEDERAL INCOME A	▼	429.8	-26	4.75	1.06†	-3.1	2.5	6.1	7.0	8.0	

* Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful.
 (o) Formerly Transamerica Special Government Inc. (p) Formerly Transamerica Government Securities A. (q) Formerly Kemper Investment Sh.-Interm. Govt. Init. (r) Formerly Kemper Investment Govt. Prem. (s) Formerly TNE Adjustable Rate U.S. Government A. (t) Formerly TNE Government Securities A. (u) Formerly TNE Limited-Term U.S. Government A. (v) Formerly Oppenheimer Govt. Securities A. (w) Formerly Thomson U.S. Government B. (x) Formerly Pioneer U.S. Government A. (y) Formerly Prudential Government Plus B.
 DATA: MORNINGSTAR INC., CHICAGO

MUTUAL FUND SCOREBOARD

Bond Funds

	RATING	SIZE ASSETS \$MIL.	% CHG 1993-94	FEES SALES CHARGE (%)	EXPENSE RATIO (%)	PERFORMANCE TOTAL RETURN (%)			PORTFOLIO		TREND 5-YEAR ANALYSIS
						1 YR	3 YR	5 YR	YIELD (%)	MATURITY (YEARS)	
U.S. GOVERNMENT INCOME A	AVG	2987.4	-33	4.75	0.85†	-2.5	3.2	6.2	7.6	8.2	
TIREMENT ACTIVELY MGD. BOND	AVG	134.7	-6	No Load	0.87	-4.2	4.4	7.5	0.0	NA	
AB S/I GOVT. BOND		160.0	-41	No Load	0.60	-2.8	3.6		5.7	2.2	
IER GNMA	◆	417.0	-32	No Load	0.95	-3.1	3.2	6.8	6.9	8.6	
A U.S. GOVERNMENT A	◆	461.4	-46	4.50	1.06†	-5.9	2.3	6.1	7.7	10.4	
BARNEY ADJUST. RATE. GOVT. A (z)		181.6	-54	No Load	2.31†	2.3			4.1	1.6	
BARNEY GOVERNMENT SEC. A (aa)		479.4	NM	4.50	1.00†	-2.9			6.1	NA	
BARNEY MANAGED GOVT. A (bb)	AVG	550.4	28	4.50	1.22†	-2.0	4.3	7.9	6.3	NA	
BARNEY U.S. GOVERNMENT A	AVG	360.7	-23	4.50	0.50	-1.5	3.8	7.3	7.6	8.0	
BREEDEN SHORT DUR. U.S. GOVT. (cc)		225.0	37	No Load	0.56	4.3			5.9	0.5	
BREEDEN SHORT DUR. U.S. GOVT. SER.		195.3	50	No Load	0.20†	4.1			5.8	0.5	
COACH GINNIE MAE A		171.3	-44	4.50	0.70†	-3.2	3.5		7.5	NA	
COACH U.S. GOVT. ALLOC. A	◆◆	140.1	-51	4.50	1.00†	-7.0	4.6	7.1	6.3	NA	
ST RESEARCH GOVT. INCOME A	AVG	608.2	-27	4.50	1.07†	-2.9	4.4	7.6	6.8	8.7	
IG GOVERNMENT SECURITIES	◆◆◆	276.8	25	No Load	0.90	-3.4	6.0	8.6	6.5	7.5	
ERICA U.S. GOVT. SEC. B	◆◆	633.1	-45	4.00**	2.12†	-1.4	2.7	5.3	5.2	NA	
IBURG LTD.-TERM U.S. GOVT. A	◆	178.9	-15	2.50	0.95†	-2.1	3.7	6.5	5.9	4.0	
ENTURY U.S. GOVT. SH-TERM (dd)	◆	383.8	-22	No Load	0.81	-0.4	2.7	5.4	4.9	1.9	
GOVERNMENT SECURITIES	AVG	1290.1	-18	4.75	0.78†	-4.6	4.3	7.2	8.0	6.2	
GOVERNMENT SECURITIES	◆	152.4	-20	4.25	0.82†	-3.9	4.3	7.3	6.2	7.7	
INVESTMENT FEDERAL GNMA		244.9	-12	No Load	0.31	0.0	4.3		7.4	4.2	
LINE U.S. GOVERNMENT	◆	289.7	-36	No Load	0.63	-10.7	1.4	6.0	7.5	5.1	
AMPEN U.S. GOVERNMENT A	◆	2917.4	-20	4.65	0.93†	-5.1	2.9	6.7	8.6	7.0	
ARD F/I GNMA	◆◆	5777.8	-18	No Load	0.31	-1.0	3.9	7.6	7.1	9.0	
ARD F/I I/T U.S. TREAS.		844.2	-14	No Load	0.29	-4.3	4.7		6.2	8.6	
ARD F/I L/T US TREAS.	◆◆	644.2	-22	No Load	0.29	-7.0	5.3	7.7	7.2	22.0	
ARD F/I S/T FEDERAL	◆◆	1504.8	-22	No Load	0.29	-0.9	4.0	6.7	5.6	2.3	
ARD F/I S/T U.S. TREAS.		704.0	0	No Load	0.29	-0.5	4.1		5.3	2.5	
RY GOVERNMENT MORTGAGE (ee)		154.4	-21	4.75	0.73	-2.1	4.0		6.8	NA	
GOVERNMENT SECURITIES	◆	216.4	-35	No Load	0.78	-8.8	2.3	5.9	7.2	6.5	

MUNICIPAL

INSURED T/F GENERAL BOND	◆◆	1748.6	-18	No Load	0.68	-6.2	4.7	6.5	5.2	16.0	
L TAX-FREE	◆	174.9	-19	4.75	0.56†	-4.6	5.5	6.5	6.1	22.3	
MUNICIPAL BOND A	AVG	257.6	-12	4.75	0.90†	-3.8	5.4	6.9	6.2	16.5	
NCE MUNI INCOME CA A	◆	437.1	-20	4.25	0.67†	-10.1	3.6	5.8	6.4	25.0	
NCE MUNI INCOME NATIONAL A	◆◆	318.9	-19	4.25	0.59†	-9.6	4.2	6.3	6.4	21.0	
NCE MUNI INCOME NY A	◆◆	171.8	-21	4.25	0.65†	-10.1	3.9	6.0	6.4	27.5	
NCE MUNI INSURED NATIONAL A	◆◆◆	150.0	-20	4.25	0.63†	-9.2	3.9	6.1	6.0	23.4	
CAN CAPITAL MUNI BOND A	AVG	295.8	-12	4.75	0.93†	-3.5	5.3	6.6	6.0	20.0	
CAN CAPITAL T/E H/Y MUNI. A	◆◆◆	418.1	1	4.75†	1.02†	0.2	6.4	7.1	7.2	20.9	
CA MUNICIPAL BOND A		171.8	-13	3.00	0.49†	-5.8	4.9		5.7	19.6	
IM CA TAX-FREE INSURED	◆	161.3	-28	No Load	0.49	-6.6	5.0	6.6	5.7	17.0	
IM CA TAX-FREE INTERM.-TERM	◆◆	393.8	-16	No Load	0.48	-3.7	4.5	6.1	5.1	6.9	
IM CA TAX-FREE LONG-TERM	AVG	249.1	-23	No Load	0.48	-6.5	4.8	6.5	6.0	18.0	
IM CA TAX-FREE SHORT-TERM		106.3	-15	No Load	0.51	-0.6			3.9	2.5	
TEIN CA MUNICIPAL		160.8	-1	No Load	0.70	-3.2	3.8		4.9	6.1	
TEIN DIVERSIFIED MUNICIPAL	◆◆	504.4	4	No Load	0.67	-2.5	4.0	5.8	4.8	11.6	
TEIN NY MUNICIPAL	◆◆	376.6	3	No Load	0.67	-2.6	4.2	5.9	5.1	14.2	
ORNIA INVMT. TAX-FREE INCOME	◆◆	185.1	-34	No Load	0.60	-8.6	4.5	6.4	5.5	17.0	
RT TAX-FREE RES. LTD.-TERM A	◆◆◆	547.6	-16	2.00	0.65	2.4	3.8	4.9	3.6	0.9	
HILL TAX-FREE OF KY	◆◆	232.8	-10	4.00	0.68†	-3.4	5.0	6.5	6.0	15.0	
IAL CA TAX-EXEMPT A	◆	295.1	-22	4.75	0.75	-7.3	3.4	5.4	6.2	23.7	
IAL HIGH-YIELD MUNICIPAL B		115.4	-6	5.00**	1.90†	-3.4			6.2	23.8	
IAL MA TAX-EXEMPT A	AVG	187.7	-16	4.75	0.64	-5.7	4.9	6.8	6.2	21.6	
IAL TAX-EXEMPT A	AVG	2837.5	-17	4.75	1.01†	-6.3	4.0	6.0	6.3	23.7	
IAL TAX-EXEMPT INSURED A	◆◆	204.8	-16	4.75	1.05†	-6.1	3.8	5.9	5.7	22.4	
IBIA MUNICIPAL BOND	◆	339.8	-21	No Load	0.58	-4.7	4.0	6.1	5.6	14.3	
ON SENSE MUNICIPAL BOND	AVG	108.4	7	4.75	0.99	-4.7	4.8	6.2	5.1	20.7	
OSITE TAX-EXEMPT BOND A	◆	215.4	-17	4.00	0.81†	-6.5	4.7	6.4	5.5	14.9	
WITTER CA TAX-FREE INCOME	◆	1006.0	-15	5.00**	1.31†	-6.0	4.0	5.5	5.3	18.0	
WITTER MULTI-STATE MUNI CA		111.4	-22	4.00	0.57†	-8.5	4.3		6.0	23.7	
WITTER NY TAX-FREE INCOME	◆	206.6	-15	5.00**	1.35†	-7.7	3.9	5.7	5.2	20.0	
WITTER TAX-EXEMPT SEC.	AVG	1292.3	-18	4.00 ‡	0.47	-5.6	4.6	6.4	6.3	18.0	
VARE TAX-FREE PA A	◆	942.6	-9	4.75	0.88†	-3.9	5.2	6.5	6.2	21.7	
VARE TAX-FREE U.S.A. A	◆◆	713.0	-7	4.75	0.89†	-3.0	5.9	6.8	6.5	22.0	
US CA INTERMEDIATE MUNI		238.4	-23	No Load	0.27	-5.5			5.4	7.6	
US CA TAX-EXEMPT BOND	AVG	1431.2	-22	No Load	0.70	-7.1	3.5	5.5	6.0	22.2	
US CT INTERMEDIATE MUNI		124.3	-11	No Load	0.25	-4.7			5.3	9.1	
US FL INTERMEDIATE MUNI		408.2	-24	No Load	0.43†	-4.9			5.2	8.9	

es redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful.
 erty Smith Barney Shearson Adj. Rate Govt. A. (aa) Formerly Smith Barney Shearson Govt. Sec. A. (bb) Formerly Smith Barney Shearson Managed Govt. A. (cc) Formerly Smith Bree-
 l. Short Dur. U.S. Govt. (dd) Formerly Twentieth Century U.S. Governments. (ee) Formerly Society U.S. Government Income.

DATA: MORNINGSTAR INC., CHICAGO, IL

MUTUAL FUND SCOREBOARD

Bond Fu

	RATING	SIZE ASSETS \$MIL	% CHG 1993-94	FEES SALES CHARGE (%)	EXPENSE RATIO (%)	PERFORMANCE TOTAL RETURN (%)			PORTFOLIO		TRI 5-Y ANA
						1 YR	3 YR	5 YR	YIELD (%)	MATURITY (YEARS)	
DREYFUS INSURED MUNICIPAL BOND	◆◆◆	215.1	-25	No Load	0.93†	-8.6	3.5	5.7	5.8	23.2	◆
DREYFUS INTERMEDIATE MUNI BOND	◆◆	1447.6	-21	No Load	0.70	-4.6	5.0	6.5	5.7	10.0	◆
DREYFUS MA TAX-EXEMPT BOND	◆	146.9	-26	No Load	0.80†	-6.0	4.3	6.3	5.9	21.7	◆
DREYFUS MUNICIPAL BOND	◆	3625.8	-21	No Load	0.68	-6.9	4.4	6.3	6.4	23.1	◆
DREYFUS NJ INTERMEDIATE MUNI	◆	212.3	-12	No Load	0.33	-5.2			5.2	8.6	◆
DREYFUS NJ MUNICIPAL BOND	◆◆	576.5	-21	No Load	0.79†	-6.0	4.9	6.9	6.2	21.0	◆
DREYFUS NY INSURED T/E BOND	AVG	151.8	-23	No Load	0.98†	-6.6	4.0	6.2	5.6	24.8	◆
DREYFUS NY TAX-EXEMPT BOND	AVG	1699.5	-20	No Load	0.71	-7.0	4.5	6.2	6.0	20.5	◆
DREYFUS NY TAX-EXEMPT INTERM. BD.	◆◆	338.0	-20	No Load	0.89†	-5.1	5.0	6.4	5.1	9.3	◆
DREYFUS SHORT-INTERM. MUNI BOND	◆◆◆	426.8	-26	No Load	0.70†	-0.3	4.3	5.5	4.5	2.2	◆
DUPREE KY TAX-FREE INCOME	◆◆◆	246.8	-9	No Load	0.69	-2.1	6.2	7.3	6.6	18.5	◆
EMERALD FL TAX-EXEMPT A		107.1	-49	4.50	0.91†	-6.9	5.5		5.3	19.8	◆
EMPIRE BUILDER TAX-FREE BOND	AVG	103.7	-5	4.25	0.98	-5.2	4.7	6.3	4.3	20.1	◆
EV MARATHON AZ TAX-FREE (ff)		137.7	-10	5.00**	1.46†	-9.7	3.9		5.8	21.7	◆
EV MARATHON CA MUNICIPALS (gg)	◆◆◆	396.4	-20	5.00**	1.67†	-9.1	2.4	4.3	6.2	21.8	◆
EV MARATHON CT TAX-FREE (HH)		176.7	-5	5.00**	1.43†	-10.4			5.9	22.5	◆
EV MARATHON FL LTD. MATURITY T/F (ii)		151.5	-8	3.00**	1.42†	-4.1			4.6	7.0	◆
EV MARATHON FL TAX-FREE (jj)		714.7	-15	5.00**	1.44†	-9.0	3.5		5.9	24.7	◆
EV MARATHON GA TAX-FREE (kk)		120.1	-14	5.00**	1.41†	-9.6	2.9		5.5	20.8	◆
EV MARATHON KY TAX-FREE (ll)		133.3	-5	5.00**	1.44†	-9.3	3.1		5.7	21.5	◆
EV MARATHON MA LTD MATURITY T/F (mm)		110.6	-6	3.00**	1.46†	-3.5			4.7	7.5	◆
EV MARATHON MA TAX-FREE (nn)		274.0	-11	5.00**	1.50†	-9.0	3.3		6.2	22.5	◆
EV MARATHON MD TAX-FREE (oo)		109.4	-3	5.00**	1.43†	-9.9			5.6	24.1	◆
EV MARATHON MI TAX-FREE (pp)		179.8	-13	5.00**	1.49†	-8.5	3.3		5.6	21.9	◆
EV MARATHON NATL LTD. MAT. T/F (qq)		145.7	-3	3.00**	1.55†	-3.2			4.9	6.6	◆
EV MARATHON NATL MUNICIPALS (rr)	◆◆	2054.7	-7	5.00**	1.51†	-8.1	5.1	6.0	6.9	25.6	◆
EV MARATHON NC TAX-FREE (ss)		178.8	-8	5.00**	1.42†	-9.3	3.0		5.7	21.3	◆
EV MARATHON NJ TAX-FREE (tt)		390.7	-10	5.00**	1.48†	-8.2	3.7		6.0	24.0	◆
EV MARATHON NY LTD. MATURITY T/F (uu)		166.6	-6	3.00**	1.40†	-4.3			4.7	7.1	◆
EV MARATHON NY TAX-FREE (vv)		606.9	-13	5.00**	1.46†	-9.4	4.0		6.1	22.0	◆
EV MARATHON OH TAX-FREE (ww)		301.2	-10	5.00**	1.50†	-8.9	3.6		5.9	20.0	◆
EV MARATHON OR TAX-FREE (xx)		137.6	-7	5.00**	1.43†	-9.5	4.0		5.6	21.1	◆
EV MARATHON PA LTD. MATURITY T/F (yy)		103.2	-7	3.00**	1.45†	-3.8			4.7	6.8	◆
EV MARATHON PA TAX-FREE (zz)		478.5	-14	5.00**	1.46†	-9.6	3.0		6.0	21.5	◆
EV MARATHON VA TAX-FREE (aaa)		178.0	-9	5.00**	1.44†	-8.9	2.9		5.8	22.0	◆
FIDELITY ADVISOR HIGH-INC MUNI A	◆◆	506.4	-6	4.75	0.89†	-8.0	5.2	7.6	6.3	20.7	◆
FIDELITY AGGRESSIVE TAX-FREE	◆◆◆	793.8	-16	1.00*	0.64	-5.9	5.4	7.0	7.1	20.2	◆
FIDELITY CA TAX-FREE HIGH-YIELD	AVG	443.9	-25	No Load	0.56	-8.9	4.0	5.8	6.5	19.6	◆
FIDELITY CA TAX-FREE INSURED	◆◆	197.3	-37	No Load	0.61	-10.2	3.7	5.8	6.0	20.2	◆
FIDELITY HIGH-YIELD TAX-FREE	AVG	1671.3	-21	No Load	0.56	-7.4	4.4	6.3	6.7	18.8	◆
FIDELITY INSURED TAX-FREE	◆	318.3	-29	No Load	0.59	-7.7	4.3	6.3	5.8	18.4	◆
FIDELITY LIMITED-TERM MUNICIPALS	◆◆	881.3	-26	No Load	0.54	-4.8	5.0	6.6	5.7	8.9	◆
FIDELITY MA TAX-FREE HIGH-YIELD	◆◆	993.8	-28	No Load	0.54	-6.6	4.9	6.6	6.0	20.2	◆
FIDELITY MI TAX-FREE HIGH-YIELD	AVG	434.4	-23	No Load	0.58	-7.5	4.9	6.3	6.4	17.4	◆
FIDELITY MN TAX-FREE	AVG	277.4	-19	No Load	0.60	-6.4	4.2	5.7	5.7	20.1	◆
FIDELITY MUNICIPAL BOND	◆	1005.6	-20	No Load	0.54	-9.1	4.0	6.1	5.6	17.4	◆
FIDELITY NY TAX-FREE HIGH-YIELD	◆	380.2	-21	No Load	0.58	-8.0	4.2	6.2	6.0	19.5	◆
FIDELITY NY TAX-FREE INSURED	◆	300.8	-27	No Load	0.59	-8.0	4.1	6.1	5.9	19.3	◆
FIDELITY OH TAX-FREE HIGH-YIELD	◆	349.5	-23	No Load	0.58	-5.5	4.9	6.7	6.1	17.7	◆
FIDELITY SPARTAN CA MUNI HI-YLD	AVG	371.9	-38	0.50*	0.55	-9.0	4.1	6.4	6.3	20.9	◆
FIDELITY SPARTAN CT MUNI HI-YLD	◆	312.8	-30	0.50*	0.55	-7.0	4.4	6.1	6.2	19.0	◆
FIDELITY SPARTAN FL MUNI INCOME		339.3	-25	0.50*	0.54	-6.7			5.9	19.4	◆
FIDELITY SPARTAN INTERM. MUNI		205.9	-26	No Load	0.20	-5.0			5.4	9.0	◆
FIDELITY SPARTAN MUNI INCOME		535.6	-38	0.50*	0.55	-8.1	4.5		6.5	19.1	◆
FIDELITY SPARTAN NJ MUNI HI-YLD	◆	325.7	-24	0.50*	0.55	-5.7	5.1	6.9	6.1	17.7	◆
FIDELITY SPARTAN NY MUNI HI-YLD		284.8	-36	0.50*	0.55	-8.5	4.4		6.1	21.1	◆
FIDELITY SPARTAN PA MUNI HI-YLD	◆◆	241.2	-21	0.50*	0.55	-5.0	5.5	7.2	6.6	18.4	◆
FIDELITY SPARTAN S/I MUNI	◆◆◆	913.1	-23	No Load	0.47	-0.1	4.5	5.7	4.6	3.5	◆
FIRST INVESTORS INSURED TAX-EX A	◆	1297.4	-13	6.25	1.21†	-6.1	3.7	5.4	5.4	20.0	◆
FIRST INVESTORS NY INSURED T/F A	◆	193.4	-8	6.25	1.31†	-5.5	4.1	5.8	5.2	21.0	◆
FLAGSHIP ALL-AMERICAN TAX-EXEMPT A	AVG	168.0	-11	4.20	0.62†	-5.9	6.0	7.6	6.3	21.5	◆
FLAGSHIP CT DOUBLE TAX-EXEMPT A	◆◆	187.9	-10	4.20	0.65†	-6.2	4.7	6.1	6.1	19.0	◆
FLAGSHIP FL DOUBLE TAX-EXEMPT A		327.1	-24	4.20	0.58†	-5.6	5.2		6.0	19.1	◆
FLAGSHIP GA DOUBLE TAX-EXEMPT A	◆	107.3	-11	4.20	0.70†	-6.1	4.2	6.1	6.0	19.3	◆
FLAGSHIP KY TRIPLE TAX-EXEMPT A	◆	354.9	-6	4.20	0.58†	-5.4	5.1	6.8	6.1	18.5	◆
FLAGSHIP LTD.-TERM TAX-EXEMPT A	◆◆◆	574.7	-17	2.50	0.70†	-1.9	5.2	6.4	4.9	4.4	◆
FLAGSHIP MI TRIPLE TAX-EXEMPT A	AVG	228.2	-10	4.20	0.75†	-5.0	5.2	6.5	6.0	16.4	◆
FLAGSHIP MO DOUBLE TAX-EXEMPT A	AVG	183.1	-3	4.20	0.62†	-6.1	5.1	6.7	6.1	19.8	◆
FLAGSHIP NC TRIPLE TAX-EXEMPT A	◆	178.5	-12	4.20	0.89†	-5.6	4.5	6.2	5.9	17.8	◆
FLAGSHIP OH DOUBLE TAX-EXEMPT A	AVG	413.8	-11	4.20	0.93†	-4.7	4.9	6.5	5.8	16.0	◆

* Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful.
 (ff) Formerly Eaton Vance AZ Tax-Free. (gg) Formerly Eaton Vance CA Municipals. (hh) Formerly Eaton Vance CT Tax-Free. (ii) Formerly Eaton Vance FL Limited Maturity Tax-Free. (jj) Form
 Eaton Vance FL Tax-Free. (kk) Formerly Eaton Vance GA Tax-Free. (ll) Formerly Eaton Vance KY T/F. (mm) Formerly Eaton Vance MA Limited Mat. T/F. (nn) Formerly Eaton Vance MA Tax
 Free. (oo) Formerly Eaton Vance MD Tax-Free. (pp) Formerly Eaton Vance MI T/F. (qq) Formerly Eaton Vance Natl. Ltd Mat. T/F.
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- Available speed sensitive steering
- Standard rear seat heat & air ducts
- Standard air conditioning with available automatic temperature control system

- Standard four-wheel independent suspension

Available 3.5L V-6, 24-valve overhead cam, 214 hp

Available Infinity Spatial Imaging™ sound system

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MUTUAL FUND SCOREBOARD

Bond F

	RATING	SIZE ASSETS \$ MIL	YIELD % (30-90)	FEES		PERFORMANCE			PORTFOLIO		T
				SALES CHARGE %	EXPENSE RATIO %	1 YR	3 YR	5 YR	YIELD %	MAT. RY YEARS	
FLAGSHIP TN DOUBLE TAX-EXEMPT A	◆	219.2	-7	4.20	0.76 ⁺	-5.5	4.8	6.4	5.9	17.8	
FLAGSHIP VA DOUBLE TAX-EXEMPT A	AVG	102.3	-7	4.20	0.64 ⁺	-5.5	5.2	6.8	6.0	20.0	
FORTRESS MUNICIPAL INCOME	AVG	413.7	-18	2.00 ⁺	1.09 ⁺	-5.7	4.2	6.0	6.0	24.9	
FRANKLIN AL TAX-FREE INCOME	◆	160.6	-10	4.25	0.68 ⁺	-4.4	5.2	6.6	6.0	22.6	
FRANKLIN AZ TAX-FREE INCOME	◆◆	692.6	-14	4.25	0.59 ⁺	-4.0	5.4	6.8	6.0	15.0	
FRANKLIN CA INSURED T F INCOME	◆	1369.1	-11	4.25	0.54 ⁺	-5.3	5.1	6.5	6.0	24.2	
FRANKLIN CA TAX-FREE INCOME	◆◆	12387.6	-12	4.25	0.55 ⁺	-2.8	5.2	6.6	6.5	23.1	
FRANKLIN CO TAX-FREE INCOME	◆	183.4	-8	4.25	0.68 ⁺	-5.4	5.4	6.8	6.1	22.1	
FRANKLIN CT TAX-FREE INCOME	◆	148.2	-9	4.25	0.70 ⁺	-5.4	4.8	6.0	6.0	21.4	
FRANKLIN FEDERAL TAX-FREE INCOME	◆◆	6561.4	-7	4.25	0.52 ⁺	-3.7	5.5	7.0	6.9	23.2	
FRANKLIN FL TAX-FREE INCOME	◆◆	1238.0	-10	4.25	0.57 ⁺	-3.4	5.6	7.0	6.1	18.0	
FRANKLIN GA TAX-FREE INCOME	◆	111.5	-6	4.25	0.73 ⁺	-3.7	5.4	6.8	5.9	22.4	
FRANKLIN HIGH-YIELD T F INCOME	◆◆◆	3124.5	-6	4.25	0.58 ⁺	-2.6	6.4	7.3	7.2	21.4	
FRANKLIN INSURED TAX-FREE INCOME	◆◆	1631.4	-10	4.25	0.57 ⁺	-3.6	5.6	6.9	6.2	21.3	
FRANKLIN MA INSURED T F INCOME	◆◆	274.6	-12	4.25	0.65 ⁺	-3.6	5.4	6.5	6.1	21.4	
FRANKLIN MD TAX-FREE INCOME	AVG	144.7	-7	4.25	0.71 ⁺	-5.1	5.0	6.5	5.9	23.8	
FRANKLIN MI INSURED T F INCOME	◆	992.9	-6	4.25	0.59 ⁺	-3.9	5.6	6.7	6.1	15.0	
FRANKLIN MN INSURED T F INCOME	◆	455.8	-9	4.25	0.65 ⁺	-3.5	5.1	6.4	6.0	17.0	
FRANKLIN MO TAX-FREE INCOME	◆	215.8	-4	4.25	0.67 ⁺	-5.1	5.4	6.9	5.9	21.5	
FRANKLIN NC TAX-FREE INCOME	AVG	204.7	-3	4.25	0.68 ⁺	-5.7	4.7	6.3	6.0	21.7	
FRANKLIN NJ TAX-FREE INCOME	◆	508.1	-8	4.25	0.62 ⁺	-5.2	4.7	6.6	6.1	19.0	
FRANKLIN NY INSURED T F INCOME	◆	225.1	-14	4.25	0.53 ⁺	-8.6	4.5		5.3	23.2	
FRANKLIN NY TAX-FREE INCOME	◆◆	4401.1	-8	4.25	0.52 ⁺	-3.6	6.2	7.4	6.8	17.0	
FRANKLIN OH INSURED T F INCOME	◆◆	625.3	-9	4.25	0.61 ⁺	-4.5	5.3	6.7	6.1	17.0	
FRANKLIN OR TAX-FREE INCOME	AVG	332.8	-11	4.25	0.64 ⁺	-4.9	4.6	6.3	5.7	20.8	
FRANKLIN PA TAX-FREE INCOME	◆◆	564.6	-8	4.25	0.61 ⁺	-3.3	5.8	6.9	6.3	17.0	
FRANKLIN PR TAX-FREE INCOME	◆	168.6	-2	4.25	0.72 ⁺	-4.3	5.0	6.5	6.3	18.0	
FRANKLIN TX TAX-FREE INCOME	◆◆	127.7	-15	4.25	0.71 ⁺	-2.8	5.5	6.9	6.1	21.0	
FRANKLIN VA TAX-FREE INCOME	◆	243.4	-5	4.25	0.67 ⁺	-4.6	5.3	6.8	6.0	22.5	
GENERAL CA MUNICIPAL BOND	◆	296.3	-32	No Load	0.76 ⁺	-7.0	4.7	6.5	6.2	22.0	
GENERAL MUNICIPAL BOND	◆	829.1	-34	No Load	0.86 ⁺	-7.3	4.9	7.3	6.2	22.4	
GENERAL NY MUNICIPAL BOND	◆	293.6	-27	No Load	0.73 ⁺	-7.2	5.3	7.3	6.1	20.0	
HANCOCK CA TAX-FREE INCOME A (bbb)	◆◆	241.0	-14	4.75	0.69 ⁺	-9.3	4.0	6.0	6.3	25.4	
HANCOCK HIGH-YIELD TAX-FREE B (ccc)	◆	149.4	25	5.00 ^{***}	2.06 ⁺	-5.7	4.4	5.8	7.0	23.9	
HANCOCK MANAGED TAX-EXEMPT B	◆◆	207.7	-19	5.00 ^{***}	1.61 ⁺	-6.0	4.9	6.4	5.1	21.8	
HANCOCK TAX-EXEMPT INCOME A	◆	467.6	-14	4.50	1.12 ⁺	-5.9	4.5	6.3	5.7	22.8	
HANCOCK TAX-FREE BOND A (ddd)	◆	114.2	-16	4.75	0.78 ⁺	-9.3	5.0		6.1	26.1	
HAWAIIAN TAX-FREE	◆	615.4	-7	4.00	0.75 ⁺	-4.6	4.3	5.8	5.9	14.6	
HEARTLAND WI TAX-FREE	◆	101.7	2	No Load	0.84 ⁺	-6.5			5.5	20.8	
IDS CA TAX-EXEMPT	◆	231.3	-18	5.00	0.61 ⁺	-5.2	4.8	6.2	6.2	22.5	
IDS HIGH-YIELD TAX-EXEMPT	AVG	5604.9	-18	5.00	0.59 ⁺	-5.0	4.2	5.9	6.9	20.5	
IDS INSURED TAX-EXEMPT	◆◆	488.6	-12	5.00	0.65 ⁺	-6.1	5.1	6.6	5.9	23.5	
IDS MN TAX-EXEMPT	AVG	373.7	-15	5.00	0.66 ⁺	-4.4	4.9	6.2	6.2	21.5	
IDS NY TAX-EXEMPT	AVG	113.5	-11	5.00	0.65 ⁺	-5.1	5.1	6.6	6.1	23.0	
IDS TAX-EXEMPT BOND	◆◆◆	1087.8	-17	5.00	0.61 ⁺	-7.4	3.8	5.6	6.2	20.4	
INVESCO TAX-FREE LONG-TERM BOND	AVG	254.1	-25	No Load	1.00 ⁺	-5.5	4.8	6.8	5.5	20.2	
KANSAS MUNICIPAL	◆	119.8	0	4.25	0.70 ⁺	-6.3	5.1		5.7	20.1	
KEMPER MUNICIPAL BOND A	◆◆	3426.7	-17	4.50	0.60 ⁺	-6.4	4.8	6.7	5.3	15.5	
KEMPER STATE TAX-FREE INC. CA A	◆	1057.3	-20	4.50	0.74 ⁺	-5.4	4.9	6.5	5.8	16.0	
KEMPER STATE TAX-FREE INC. FL A	◆	119.8	-14	4.50	0.79 ⁺	-3.9	6.0		5.4	20.3	
KEMPER STATE TAX-FREE INC. NY A	◆	305.7	-19	4.50	0.76 ⁺	-4.9	5.6	7.2	5.7	15.2	
KEYSTONE TAX-EXEMPT	◆◆	679.7	-18	4.00 ^{**}	1.66 ⁺	-7.1	3.3	5.2	5.9	19.2	
KEYSTONE TAX-FREE	◆	1197.7	-22	4.00 ^{***}	1.57 ⁺	-7.3	3.5	5.5	6.1	19.9	
LEGG MASON MD TAX-FREE INCOME	◆	134.1	-14	2.75	0.46 ⁺	-3.3	5.2		5.2	13.4	
LIBERTY FINANCIAL TAX-FREE BOND	AVG	224.5	-18	4.50	0.57 ⁺	-4.6	4.9	6.5	5.9	19.2	
LIBERTY MUNICIPAL SECURITIES A	◆	674.7	-14	4.50	0.84 ⁺	-3.8	4.8	6.5	6.2	25.2	
LIMITED TERM NY MUNICIPAL	◆	494.3	8	2.00	0.88 ⁺	-0.5	6.6		5.2	4.7	
LIMITED TERM TAX-EXEMPT BOND AMER.	◆	182.4	36	4.75	NA ⁺	-2.9			4.8	11.0	
LORD ABBETT CA TAX-FREE INCOME	◆◆◆	290.2	-21	4.75	0.67 ⁺	-10.5	3.7	6.3	6.3	19.4	
LORD ABBETT TAX-FREE INCOME CT	◆	101.2	2	4.75	0.49 ⁺	-7.4	4.5		6.8	18.1	
LORD ABBETT TAX-FREE INCOME FL	◆	171.7	-13	4.75	0.38 ⁺	-8.2	4.8		6.6	20.4	
LORD ABBETT TAX-FREE INCOME MO	◆	116.7	1	4.75	0.60 ⁺	-8.7	4.4		6.6	18.3	
LORD ABBETT TAX-FREE INCOME NATL	◆◆	614.6	-14	4.75	0.86 ⁺	-7.9	4.3	6.5	6.8	18.8	
LORD ABBETT TAX-FREE INCOME NJ	◆	176.1	-7	4.75	0.51 ⁺	-6.4	5.4		6.6	18.8	
LORD ABBETT TAX-FREE INCOME NY	◆◆◆	317.0	-17	4.75	0.83 ⁺	-8.9	3.9	6.3	6.7	22.0	
MACKENZIE LIMITED-TERM MUNI A	◆	124.0	-8	3.00	0.88 ⁺	-2.2	3.6		6.0	5.9	
MAINSTAY TAX-FREE BOND B	◆	513.6	-2	5.00 ^{**}	1.20 ⁺	-6.0	4.0	5.5	5.6	22.7	
MERRILL LYNCH CA MUNI BOND B	◆◆	623.5	-23	4.00 ^{**}	1.13 ⁺	-7.5	3.9	5.5	5.7	24.0	
MERRILL LYNCH FL MUNI BOND B	◆	200.1	-14	4.00 ^{**}	1.18 ⁺	-8.4	3.4		5.1	24.0	
MERRILL LYNCH MUNI INSURED B	◆◆◆	752.5	-22	4.00 ^{**}	1.17 ⁺	-7.4	3.9	5.8	5.1	20.6	



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MUTUAL FUND SCOREBOARD

Bond Fund

	RATING	SIZE ASSETS \$MIL	% CHG 1993-94	FEES		PERFORMANCE			PORTFOLIO		TRE 5-YR ANALY
				SALES CHARGE (%)	EXPENSE RATIO (%)	TOTAL RETURN (%)			YIELD (%)	MATURITY (YEARS)	
						1 YR	3 YR	5 YR			
MERRILL LYNCH MUNI INTERM.-TERM B	AVG	128.2	-18	1.00**	1.04†	-4.1	4.5	5.9	5.0	10.2	
MERRILL LYNCH MUNI LTD. MATURITY B		156.8	14	1.00**	0.76†	0.9			3.4	2.7	
MERRILL LYNCH MUNI NATIONAL B	♦♦	401.8	-17	4.00**	1.30†	-7.4	3.9	5.6	5.3	21.3	
MERRILL LYNCH NJ MUNI BOND B		158.1	-17	4.00**	1.20†	-6.5	3.9		5.1	20.0	
MERRILL LYNCH NY MUNI BOND B	♦♦	582.9	-20	4.00**	1.13†	-9.1	3.6	5.5	5.5	20.3	
MERRILL LYNCH PA MUNI BOND B		117.2	-9	4.00**	1.25†	-6.0	4.9		5.2	18.0	
METLIFE-STATE ST RES T/E A (eee)	♦♦♦	237.5	-22	4.50	1.21†	-6.9	4.5	6.0	5.1	18.7	
MFS AR MUNICIPAL BOND A		177.9	-10	4.75	0.67†	-6.1			5.7	18.9	
MFS CA MUNICIPAL BOND A	♦♦	258.5	-26	4.75	0.69†	-8.1	4.2	6.3	6.0	16.5	
MFS MA MUNICIPAL BOND A	♦	248.9	-16	4.75	1.16†	-5.6	4.4	6.4	6.2	17.2	
MFS MD MUNICIPAL BOND A	♦♦	141.6	-17	4.75	1.20†	-6.1	3.6	5.5	5.7	17.5	
MFS MUNICIPAL BOND A	♦♦	1886.6	-14	4.75	0.59	-6.9	5.0	6.8	5.4	18.7	
MFS MUNICIPAL HIGH-INCOME A	♦	896.3	12	4.75†	1.03	-2.9	4.8	5.6	8.0	22.0	
MFS MUNICIPAL INCOME B	AVG	419.8	-20	4.00**	2.12†	-5.3	4.3	5.5	5.2	18.7	
MFS NC MUNICIPAL BOND A	♦♦	412.1	-15	4.75	1.16†	-6.3	3.6	5.6	5.6	18.2	
MFS NY MUNICIPAL BOND A	AVG	143.3	-21	4.75	1.04†	-6.1	5.3	7.1	5.7	18.4	
MFS SC MUNICIPAL BOND A	♦	160.0	-13	4.75	1.17†	-5.7	4.3	6.1	5.5	18.4	
MFS TN MUNICIPAL BOND A	AVG	111.9	-7	4.75	1.21†	-4.1	4.7	6.2	5.6	19.2	
MFS VA MUNICIPAL BOND A	♦	409.8	-13	4.75	1.15†	-6.7	3.6	5.7	5.8	16.7	
MFS WV MUNICIPAL BOND A	AVG	120.6	-13	4.75	1.21†	-5.3	4.6	6.3	5.8	18.1	
NATIONWIDE TAX-FREE INCOME	♦♦	237.3	-9	5.00**	0.99†	-9.1	3.9	5.7	5.5	21.0	
NEW ENGLAND MA TAX-FREE INC. A (fff)		108.0	-16	4.25	0.85†	-7.4	4.3	5.9	6.0	11.0	
NEW ENGLAND T/E INCOME A (ggg)	♦♦♦	184.4	-19	4.50	0.93†	-8.1	4.1	5.7	5.8	20.0	
NEW YORK MUNI	♦♦♦	213.2	-22	No Load	2.89†	-20.4	0.1	2.8	6.4	18.3	
NUVEEN CA INSURED TAX-FREE VAL. R	♦	187.3	-10	No Load†	0.67	-6.9	4.6	6.3	5.8	23.9	
NUVEEN CA TAX-FREE VALUE R	AVG	197.1	-10	No Load†	0.73	-6.5	4.4	6.0	6.1	20.2	
NUVEEN INSURED MUNICIPAL BOND R	AVG	693.0	-7	No Load†	0.65	-6.3	5.2	7.0	5.9	20.2	
NUVEEN MUNICIPAL BOND	♦♦	2590.8	-3	4.75	0.60	-1.8	5.0	6.2	5.9	19.0	
NUVEEN NY INSURED TAX-FREE VAL R	AVG	330.2	-16	No Load†	0.65	-6.1	5.2	6.8	5.7	21.7	
NUVEEN NY TAX-FREE VALUE R	♦	139.6	-2	No Load†	0.74	-6.0	5.5	6.8	5.9	23.5	
NUVEEN OH TAX-FREE VALUE R	♦	154.4	-8	No Load†	0.71	-5.2	5.4	6.9	5.8	20.8	
OPPENHEIMER CA TAX-EXEMPT A	♦♦	219.9	-17	4.75	0.97†	-8.5	4.0	5.8	6.4	22.0	
OPPENHEIMER NY TAX-EXEMPT A	♦♦	625.9	-19	4.75	0.86†	-8.8	4.2	6.1	6.2	18.5	
OPPENHEIMER TAX-FREE BOND A	♦♦♦	541.2	-11	4.75	0.88†	-9.3	4.1	6.0	6.2	20.5	
OVERLAND EXPRESS CA TAX-FREE BD. A	♦	273.1	-25	4.50	0.48†	-4.3	5.6	7.0	6.2	16.9	
PACIFIC HORIZON CA TAX-EXEMPT BD.	♦	187.9	-24	4.50	0.93	-5.7	4.8	6.3	6.0	18.1	
PACIFICA CA TAX-FREE		150.3	-34	4.50	0.87†	-6.3	4.3		5.4	15.1	
PAINEWEBBER CA TAX-FREE INCOME A	♦♦♦	172.1	-27	4.00	0.90†	-8.1	3.4	5.5	5.8	22.7	
PAINEWEBBER NATL. TAX-FREE INC. A	♦♦♦	335.5	-24	4.00	0.89†	-7.1	4.1	5.9	5.8	22.0	
PARAGON LA TAX-FREE	♦♦	195.3	-1	4.50	0.64	-3.2	4.9	6.4	5.2	9.6	
PHOENIX CA TAX-EXEMPT BONDS A	AVG	113.0	-22	4.75	0.85†	-5.2	3.5	5.8	6.1	18.4	
PHOENIX TAX-EXEMPT BOND A	♦♦	140.5	-19	4.75	1.03†	-7.4	5.2	6.6	6.3	15.6	
PIERPONT TAX-EXEMPT BOND	♦	331.2	-33	No Load	0.71	-3.6	3.9	5.9	3.9	7.4	
PIONEER TAX-FREE INCOME	♦	452.7	-15	4.50	0.90†	-6.4	4.8	6.8	5.7	22.8	
PIPER JAFFRAY MN TAX-EXEMPT	♦	137.5	-19	4.00	0.93†	-5.6	4.6	6.2	6.0	18.9	
PREMIER CA MUNICIPAL BOND A	AVG	187.4	-23	4.50	0.87†	-6.0	4.9	6.7	6.0	20.1	
PREMIER MUNICIPAL BOND A	♦	485.3	-19	4.50	0.85†	-6.4	5.6	7.6	6.4	22.3	
PREMIER NY MUNICIPAL BOND A	♦	138.5	-17	4.50	0.87†	-6.8	5.4	7.1	5.6	20.6	
PREMIER STATE MUNI BOND CT A	♦	324.5	-18	4.50	0.80†	-5.7	4.9	6.5	5.9	22.4	
PREMIER STATE MUNI BOND FL A	AVG	249.8	-22	4.50	0.80†	-4.5	5.2	7.1	5.9	21.7	
PREMIER STATE MUNI BOND MD A	AVG	295.1	-20	4.50	0.80†	-4.7	4.8	6.8	5.9	22.0	
PREMIER STATE MUNI BOND MI A	♦	169.7	-16	4.50	0.81†	-4.6	5.8	7.3	5.9	20.2	
PREMIER STATE MUNI BOND MN A	♦	142.4	-14	4.50	0.80†	-4.4	5.2	7.0	5.9	21.2	
PREMIER STATE MUNI BOND OH A	♦♦	267.4	-16	4.50	0.81†	-4.1	5.6	7.2	6.0	20.5	
PREMIER STATE MUNI BOND PA A	♦	210.9	-15	4.50	0.81†	-5.3	5.4	7.4	6.0	21.2	
T. ROWE PRICE CA TAX-FREE BOND	♦	122.2	-21	No Load	0.60	-5.7	4.9	6.5	5.7	17.2	
T. ROWE PRICE MD TAX-FREE BOND	♦	675.2	-18	No Load	0.57	-5.0	5.1	6.5	5.9	16.0	
T. ROWE PRICE NY TAX-FREE BOND	♦	110.8	-18	No Load	0.60	-5.9	5.6	6.9	5.8	16.6	
T. ROWE PRICE TAX-FREE HIGH-YIELD	♦♦♦	802.2	-16	No Load	0.79	-4.4	5.8	7.2	6.5	19.6	
T. ROWE PRICE TAX-FREE INCOME	AVG	1253.9	-16	No Load	0.59	-5.5	5.3	6.7	6.0	16.8	
T. ROWE PRICE TAX-FREE SH. INTRM.	♦♦♦	451.1	-16	No Load	0.59	0.3	4.2	5.3	4.2	2.8	
T. ROWE PRICE VA TAX-FREE BOND		143.9	-12	No Load	0.65	-5.1	5.3		5.6	17.8	
PRINCOR TAX-EXEMPT BOND A	♦♦♦	161.1	-11	5.00	0.91†	-9.4	3.7	5.7	6.0	24.7	
PRUDENTIAL CA MUNI CA B	♦	161.9	-24	5.00**	1.13†	-6.2	4.3	5.8	5.6	17.8	
PRUDENTIAL MUNI BOND HIGH-YIELD B	♦♦	975.2	-17	5.00**	1.09†	-3.4	5.1	6.2	6.5	13.1	
PRUDENTIAL MUNI BOND INSURED B	♦♦	615.6	-26	5.00**	1.11†	-5.7	4.3	6.1	5.0	18.7	
PRUDENTIAL MUNICIPAL FL A		121.7	-21	3.00	0.20†	-7.2	4.9		6.2	20.5	
PRUDENTIAL MUNICIPAL NJ B	AVG	279.6	-23	5.00**	0.98†	-6.4	4.6	6.4	5.4	19.1	
PRUDENTIAL MUNICIPAL NY B	AVG	300.9	-18	5.00**	1.14†	-6.8	4.9	6.3	5.4	18.4	
PRUDENTIAL MUNICIPAL OH B	AVG	108.3	-14	5.00**	1.24†	-5.2	4.8	6.3	5.4	16.0	

* Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful. Δ = Existing shareholders only, new shareholders will have to pay sales charges. (eee) Formerly MetLife-State Street Tax-Exempt A. (fff) Formerly TNE MA Tax-Free Income A. (ggg) Formerly TNE MA Tax-Free Income A.

DATA: MORNINGSTAR INC., CHICAGO

MUTUAL FUND SCOREBOARD

Bond Funds

	RATING	SIZE ASSETS \$ MIL.	% CHG. 1993-94	FEES		PERFORMANCE			PORTFOLIO		TREND 5-YEAR ANALYSIS
				SALES CHARGE (%)	EXPENSE RATIO (%)	TOTAL RETURN (%)			YIELD (%)	MATURITY (YEARS)	
						1 YR	3 YR	5 YR			
NTIAL MUNICIPAL PA B	♦	234.8	-15	5.00**	1.15†	-6.4	4.8	6.1	5.6	18.5	
NTIAL NATIONAL MUNICIPALS B	♦	670.9	-21	5.00**	1.13†	-6.4	4.4	6.3	5.2	17.8	
M AZ TAX EXEMPT INCOME A		129.3	-16	4.75	0.97†	-6.7	4.4		6.0	21.1	
M CA TAX EXEMPT INCOME A	♦	3002.9	-18	4.75	0.68†	-6.7	4.6	6.4	6.3	22.1	
M FL TAX EXEMPT INCOME A		262.7	-15	4.75	0.91†	-6.2	4.6		5.9	21.9	
M MA TAX EXEMPT INCOME II A	♦♦	227.3	-12	4.75	0.96†	-6.1	5.3	7.3	6.3	21.9	
M MI TAX EXEMPT INCOME II A	AVG	122.4	-6	4.75	0.99†	-5.4	4.7	6.4	6.1	22.6	
M MUNICIPAL INCOME A	♦	784.3	-11	4.75	0.97†	-6.4	5.3	6.9	6.5	21.6	
M NJ TAX EXEMPT INCOME A		224.3	-14	4.75	0.95†	-6.3	4.6		6.1	23.5	
M NY TAX EXEMPT INCOME A	♦♦♦	1917.8	-17	4.75	0.76†	-7.4	5.0	6.6	6.1	23.2	
M NY TAX EXEMPT OPPORT. A		164.8	-8	4.75	0.98†	-2.8	4.8		6.5	23.1	
M OH TAX EXEMPT INCOME II A	♦♦	182.5	-8	4.75	0.99†	-4.8	5.0	6.5	6.2	20.8	
M PA TAX EXEMPT INCOME A	♦♦	162.0	-6	4.75	0.94†	-4.8	5.4	7.3	6.1	20.5	
M TAX EXEMPT INCOME A	♦♦♦	2123.6	-14	4.75	0.77†	-7.9	4.9	6.4	6.5	23.0	
M TAX FREE HIGH YIELD B	♦♦	1378.3	-7	5.00**	1.45†	-5.9	5.4	6.3	6.4	23.0	
M TAX FREE INSURED B	♦♦	386.4	-15	5.00**	1.53†	-6.4	3.7	5.4	5.2	22.2	
STER FUND MUNICIPALS	♦	1793.9	0	4.00	0.75†	-8.3	5.3	7.2	7.0	16.3	
O MUNICIPAL BOND	♦♦	434.4	-24	No Load	0.55	-8.2	4.0	6.4	6.2	21.2	
ER CA TAX-FREE	AVG	274.4	-22	No Load	0.80	-7.3	4.9	6.7	5.3	15.5	
ER HIGH-YIELD TAX-FREE	AVG	259.8	-18	No Load	0.80	-8.4	5.0	6.8	6.1	18.0	
ER MA TAX-FREE	♦	277.5	-26	No Load	0.33	-6.2	5.9	7.2	6.0	15.8	
ER MANAGED MUNICIPAL BONDS	AVG	708.4	-22	No Load	0.63	-6.0	5.1	6.8	5.7	16.0	
ER MEDIUM-TERM TAX-FREE	♦♦♦	703.1	-31	No Load	0.56	-3.5	5.3	6.8	5.3	8.5	
ER NY TAX-FREE	♦	182.1	-20	No Load	0.83	-7.2	4.9	6.6	5.3	16.7	
IAN TAX-EXEMPT MA A	AVG	112.0	-17	4.75	0.85†	-4.4	5.2	6.7	5.8	18.5	
IAN TAX-EXEMPT MI A	♦	144.2	-12	4.75	0.84†	-4.8	5.1	6.6	5.7	18.0	
IAN TAX-EXEMPT MN A	AVG	130.2	-10	4.75	0.85†	-2.5	5.5	6.1	6.0	15.3	
IAN TAX-EXEMPT NATIONAL A	♦♦♦	107.7	-18	4.75	0.85†	-9.9	3.5	5.5	5.8	27.0	
IAN TAX-EXEMPT OH A	AVG	164.3	-13	4.75	0.84†	-4.9	4.8	6.4	5.7	18.2	
IAN TAX-EXEMPT SC A	♦♦♦	106.8	-16	4.75	0.83†	-6.7	4.1	6.0	5.6	18.6	
CA MUNICIPAL A	♦♦	398.5	-32	4.50	0.79†	-8.6	4.3	5.8	6.2	21.7	
NATIONAL MUNICIPAL A		274.4	-33	4.50	0.87†	-7.0	5.6		6.2	19.4	
C-FREE INCOME	♦♦♦	243.3	-29	No Load	0.79	-0.6	5.7	6.7	6.0	14.3	
BARNEY CA MUNICIPALS A (hhh)	♦	362.1	-14	4.00	0.79†	-6.7	4.3	6.2	6.1	22.0	
BARNEY MANAGED MUNIS A (iii)	AVG	1606.9	-10	4.00	0.72†	-4.5	6.6	7.8	6.4	24.9	
BARNEY MUNI CA A	AVG	154.2	-14	4.00	0.51†	-5.7	4.6	6.6	6.5	18.3	
BARNEY MUNI FL A		103.4	-9	4.00	0.54†	-5.1	5.3		6.2	18.2	
BARNEY MUNI NATIONAL A	AVG	387.4	-13	4.50	0.52†	-5.8	5.3	7.1	6.7	22.9	
BARNEY NJ MUNICIPALS A (jjj)	AVG	106.2	-18	4.00	0.87†	-7.1	4.7	6.9	5.8	21.0	
BARNEY NY MUNICIPALS A (kkk)	AVG	463.8	-19	4.00	0.78†	-6.7	4.2	6.1	6.3	23.1	
BARNEY TAX-EXEMPT INC. B (iii)	AVG	731.3	-37	4.50**	1.33†	-6.5	4.3	5.8	5.9	18.8	
DOACH CA TAX-FREE BOND A		305.8	-43	4.50	0.65†	-7.3	4.7		5.7	17.2	
OE HIGH-YIELD MUNICIPALS	AVG	266.6	-24	No Load	0.76	-4.2	3.7	5.7	5.9	18.9	
OE INTERMEDIATE MUNICIPALS	♦♦	215.6	-17	No Load	0.71	-3.5	4.8	6.5	4.8	8.7	
OE MANAGED MUNICIPALS	♦	604.7	-23	No Load	0.65	-5.5	4.3	6.7	5.8	16.7	
S HIGH-YIELD MUNI BOND		107.6	416	No Load	0.00	-1.0			7.7	17.1	
S MUNICIPAL BOND	♦♦	279.8	-30	No Load	0.80	-4.6	6.2	7.3	6.1	19.4	
S SHORT-TERM MUNICIPAL BOND		161.2	-25	No Load	0.70	-1.5	4.1		4.8	2.9	
ERICA TAX-EXEMPT INSURED A	AVG	135.9	-27	4.75	1.22†	-4.0	3.4	4.9	5.6	17.0	
EMPT BOND FUND OF AMERICA	AVG	1253.1	-11	4.75	0.69†	-4.8	5.1	6.5	6.1	20.3	
EMPT FUND OF CA	♦	207.8	-10	4.75	0.71†	-5.1	5.1	6.2	5.8	22.2	
EE FUND OF CO	♦♦	199.3	-10	4.00	0.54†	-3.8	5.2	6.6	5.6	10.6	
EE TRUST OF AZ	♦	357.6	-8	4.00	0.70†	-5.3	4.8	6.4	5.8	13.6	
EE TRUST OF OR	♦	297.9	-12	4.00	0.68	-3.8	4.5	6.2	5.6	15.8	
BURG INTERMEDIATE MUNI A		208.7	10	3.50	0.90†	-2.5	6.3		5.4	8.6	
BURG LTD.-TERM MUNI CA A	♦♦♦	109.7	23	2.50	1.00†	-2.1	4.4	5.5	4.8	4.9	
BURG LTD.-TERM MUNI NATL A	♦♦♦	1019.2	12	2.50	0.95†	-1.5	4.9	6.0	4.9	4.4	
BURG NM INTERMEDIATE MUNI A		146.1	13	3.50	0.83†	-1.9	5.5		4.8	10.4	
MUNICIPAL BOND	♦♦♦	897.8	-16	4.25	0.64†	-7.1	5.2	6.9	5.7	17.8	
MUNICIPAL HIGH-INCOME	♦♦♦	339.5	1	4.25	0.76†	-3.1	6.5	7.7	6.9	21.6	
AX-EXEMPT CA BOND	♦♦	335.2	-22	No Load	0.44	-9.3	3.5	5.8	6.2	22.9	
AX-EXEMPT INTERM.-TERM	♦♦	1416.1	-15	No Load	0.40	-4.0	5.1	6.6	5.7	8.8	
AX-EXEMPT LONG-TERM	AVG	1661.2	-18	No Load	0.39	-7.9	4.5	6.4	6.3	23.2	
AX-EXEMPT SHORT-TERM	♦♦♦	810.8	-15	No Load	0.42	0.8	4.1	5.1	4.4	2.8	
AX-EXEMPT VA BOND		215.5	-15	No Load	0.49	-6.3	4.6		6.1	21.7	
STER INTERM-TERM T/E (mmm)	♦	228.0	-25	4.50	0.64	-4.2	4.8	6.2	4.1	8.2	
LINE TAX-EXEMPT HIGH-YIELD	♦	225.9	-22	No Load	0.59	-6.9	3.8	6.0	5.7	18.8	
MPEN CA INSURED TAX-FREE A	♦♦	130.3	-13	3.00	0.67†	-8.6	4.8	6.4	5.8	17.7	
MPEN INSURED T/F INCOME A	♦♦	1186.6	-3	4.65	0.79†	-6.3	4.8	6.4	6.0	19.0	
MPEN MUNICIPAL INCOME A		494.9	-17	4.65	0.97†	-6.4	4.8		6.2	21.5	

† redemption fee. ** Includes deferred sales charge. ‡ 12(b)-1 plan in effect. † Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful.
 Formerly Smith-Barney Shearson CA Municipals A. (iii) Formerly Smith Barney Shearson Managed Munis A. (jjj) Formerly Smith Barney Shearson NJ Municipals A. (kkk) Formerly Smith
 Shearson NY Municipals A. (lll) Formerly Smith Barney Shearson Tax-Ex. Income B. (mmm) Formerly UST Master Interim.-Term Tax-Ex. Non-Plan.

DATA: MORNINGSTAR INC., CHICAGO, IL

MUTUAL FUND SCOREBOARD

Bond Funds

	RATING	SIZE ASSETS \$ MIL.	% CHG. 1993-94	FEES		PERFORMANCE TOTAL RETURN (%)			PORTFOLIO		TRAILING 5-YR ANNUAL
				SALES CHARGE (%)	EXPENSE RATIO (%)	1 YR	3 YR	5 YR	YIELD (%)	MATURITY (YEARS)	
VAN KAMPEN PA TAX-FREE INCOME A	AVG	202.8	-8	4.65	0.82†	-5.7	5.5	7.1	6.0	20.8	
VAN KAMPEN TAX-FREE HIGH-INCOME A	♦	601.4	-5	4.65	0.91†	-4.9	3.3	4.3	7.4	20.0	
VANGUARD CA TAX-FR INS LONG-TERM	♦♦	830.2	-24	No Load	0.20	-5.7	5.2	6.7	6.0	17.4	
VANGUARD FL INSURED TAX-FREE		328.1	5	No Load	0.21	-4.7			5.6	17.2	
VANGUARD MUNI BOND HIGH-YIELD	AVG	1572.6	-17	No Load	0.20	-5.1	5.5	7.4	6.4	17.8	
VANGUARD MUNI BOND INSURED L/T	♦	1738.0	-20	No Load	0.20	-5.6	5.2	7.0	6.1	16.7	
VANGUARD MUNI BOND INTERM.-TERM	♦♦♦	4585.0	-12	No Load	0.20	-2.1	5.9	7.4	5.5	8.4	
VANGUARD MUNI BOND LIMITED-TERM	♦♦♦	1629.5	-10	No Load	0.20	0.1	4.2	5.8	4.4	2.6	
VANGUARD MUNI BOND LONG-TERM	♦	920.3	-17	No Load	0.20	-5.8	5.3	7.2	6.1	17.4	
VANGUARD MUNI BOND SHORT-TERM	♦♦♦	1483.5	1	No Load	0.20	1.6	3.4	4.8	3.6	1.2	
VANGUARD NJ TAX-FREE INS. LONG TERM	♦	583.9	-24	No Load	0.22	-5.2	5.5	7.1	5.9	15.1	
VANGUARD NY INSURED TAX-FREE	AVG	699.0	-15	No Load	0.22	-5.6	5.4	7.0	5.9	15.1	
VANGUARD OH TAX-FREE INS. LONG TERM		147.1	-15	No Load	0.23	-5.1	5.4		5.7	14.9	
VANGUARD PA TAX-FREE INS. LONG TERM	♦	1299.3	-15	No Load	0.21	-4.5	5.8	7.3	6.1	15.3	
VENTURE MUNI (-) PLUS B	♦♦♦	143.2	-22	4.00**	2.08†	2.3	6.3	6.6	6.6	15.9	
VOYAGEUR AZ INSURED TAX-FREE A		231.7	-12	4.75	0.69†	-7.4	4.6		5.7	19.5	
VOYAGEUR CO TAX-FREE A	♦	354.2	-11	3.90	0.71	-9.1	4.5	6.2	6.0	20.7	
VOYAGEUR FL INSURED TAX-FREE A		240.2	-22	4.75	0.38†	-8.7			5.9	23.2	
VOYAGEUR MN INSURED A	♦	284.1	-9	4.75	0.74†	-7.9	4.4	6.2	5.7	20.7	
VOYAGEUR MN TAX-FREE A	♦	406.5	-11	4.75	0.92†	-6.7	4.3	6.1	5.7	20.3	

INTERNATIONAL

ALLIANCE MULTI-MARKET STRATEGY B		186.1	-54	3.00**	2.06†	-13.3	-2.6		8.4	NA	
ALLIANCE NORTH AMER. GOVT. INC. B		1152.8	-22	3.00**	2.07†	-30.8			14.3	NA	
ALLIANCE SHORT-TERM MULTI-MKT B		816.3	-50	3.00**	1.83†	-9.4	-1.2		7.3	1.3	
AMERICAN CAPITAL GLOBAL GOVT. B		127.8	15	4.00**	2.22†	-6.9	2.2		7.4	NA	
BENHAM EUROPEAN GOVERNMENT BOND		193.7	-46	No Load	0.87	1.5			5.8	6.3	
BLANCHARD SHORT-TERM GLOBAL INC.		305.7	-52	No Load	1.44†	-4.6	2.4		6.4	1.2	
CAPITAL WORLD BOND	♦	563.2	7	4.75	1.11†	-1.4	5.1	8.3	6.4	11.2	
DEAN WITTER GLOBAL S/T INC.		148.3	-47	3.00**	1.64†	0.1	2.7		6.3	NA	
DEAN WITTER WORLD WIDE INCOME	♦♦	164.5	-38	5.00**	1.91†	-4.4	2.7	5.0	5.4	3.6	
EV MARATHON S/T STRAT. INCOME (nnn)		211.0	-42	3.00**	2.10†	-5.3	1.4		7.6	NA	
FIDELITY GLOBAL BOND	♦♦♦	382.9	-44	No Load	1.20	-16.7	1.7	5.9	6.5	8.3	
FIDELITY NEW MARKETS INCOME		179.5	-37	No Load	1.28	-16.5			5.4	9.5	
FIDELITY SHORT-TERM WORLD INCOME		265.8	-36	No Load	1.07	-5.9	3.5		7.9	1.1	
FRANKLIN GLOBAL GOVT. INCOME	♦♦♦	176.5	-16	4.25	0.89†	-7.8	2.9	6.0	9.2	8.0	
G.T. GLOBAL GOVERNMENT INCOME A	♦♦♦	458.8	-36	4.75	1.29†	-14.4	3.1	6.2	7.5	6.3	
G.T. GLOBAL HIGH-INCOME B		209.5	23	5.00**	2.64†	-19.6			8.9	10.0	
G.T. GLOBAL STRATEGIC INCOME B		403.8	-6	5.00**	2.19†	-21.3			8.6	10.8	
GOLDMAN SACHS GLOBAL INCOME		346.8	-49	4.50	1.28†	-5.3	4.7		6.3	NA	
IDS GLOBAL BOND	♦	449.8	41	5.00	1.26	-6.3	6.1	9.2	3.5	12.1	
INTERNATIONAL INCOME A		198.5	-15	4.50	1.30†	-4.6	6.1		5.7	7.3	
KEMPER GLOBAL INCOME A	♦	119.8	44	4.50	1.65	-1.5	2.1	7.7	7.0	NA	
LEGG MASON GLOBAL GOVERNMENT		145.1	-10	No Load	0.98†	-1.6			6.2	7.4	
LORD ABBETT GLOBAL INCOME	♦♦	249.5	-10	4.75	1.04†	-3.4	4.4	7.8	9.1	7.3	
MERRILL LYNCH GLOBAL BOND B	♦	701.0	-22	4.00**	1.60†	-6.2	3.7	8.1	5.1	5.2	
MERRILL LYNCH S/T GLOB. INC. B		640.0	-58	4.00**	1.45†	-3.5	-0.3		5.7	NA	
MFS WORLD GOVERNMENTS A	♦♦	358.8	-19	4.75	1.58†	-6.6	3.9	8.4	1.4	5.0	
PAINWEBBER GLOBAL INCOME B	AVG	660.3	-44	5.00**	1.96†	-4.7	2.7	7.2	5.8	4.9	
T. ROWE PRICE INTERNATIONAL BOND	♦	738.1	-1	No Load	0.99	-1.8	6.5	10.5	6.3	7.2	
PRUDENTIAL INTERM GLOBAL INC. A	♦♦♦	207.6	-35	3.00	1.45†	-7.0	3.7	5.0	6.9	NA	
PRUDENTIAL S/T GLOBAL INC. B		165.0	-52	3.00**	1.99†	-5.2	0.1		5.9	NA	
PUTNAM GLOBAL GOVERNMENTAL INC. A	♦♦	428.7	-26	4.75	1.29†	-10.0	2.2	7.4	7.0	11.8	
SCUDDER INTERNATIONAL BOND	♦	1086.2	-20	No Load	1.27	-8.6	4.4	11.0	8.7	8.0	
SCUDDER S/T GLOBAL INCOME		496.9	-47	No Load	1.00	-1.1	3.6		8.2	2.3	
SIERRA SHORT-TERM GLOBAL GOVT. A		152.6	-34	3.50	0.85†	-1.2			6.8	NA	
TCW/DW NORTH AMERICAN GOVT. INC.		880.9	-69	No Load	1.51†	-15.6			8.5	NA	
TEMPLETON INCOME	♦♦♦	198.6	-8	4.25	1.18†	-3.6		6.7	7.6	6.8	
VAN ECK GLOBAL INCOME A (ooo)	♦♦♦	137.1	-46	4.75	1.35†	-2.8	-0.5	6.6	6.8	NA	
VAN KAMPEN SH-TERM GLOBAL INC. B		185.4	-50	3.00**	1.85†	-8.1	0.8		7.5	2.0	

CONVERTIBLE

AMERICAN CAPITAL HARBOR A	♦♦♦	369.9	-14	5.75	1.32†	-6.4	5.3	7.2	4.6	11.4	
DEAN WITTER CONVERTIBLE	♦♦♦	175.0	-15	5.00**	1.93†	-2.9	6.7	6.1	4.0	NA	
FIDELITY CONVERTIBLE SECURITIES	AVG	891.3	-16	No Load	0.87	-1.8	12.2	13.7	5.2	NA	
MAINSTAY CONVERTIBLE B	♦	180.2	133	5.00**	1.90†	-1.3	11.6	14.0	4.0	12.0	
PACIFIC HORIZON CAPITAL INCOME	♦♦	200.6	30	4.50	1.09	-5.9	11.9	13.1	4.4	8.8	
PHOENIX CONVERTIBLE A	♦♦	211.7	-14	4.75	1.14†	-3.8	6.1	7.0	4.8	NA	
PRUDENTIAL INCOMEVERTIBLE B	♦♦♦	231.1	-25	5.00**	2.12†	-4.2	4.8	5.3	3.3	NA	
PUTNAM CONVERTIBLE INC. GRTH. A	♦♦♦	667.0	-5	5.75	0.99†	-1.9	11.6	10.1	5.3	NA	

* Includes redemption fee. ** Includes deferred sales charge. † 12(b)-1 plan in effect. ‡ Not currently accepting new accounts or deposits. NA = Not available. NM = Not meaningful. (nnn) Formerly Eaton Vance Short-Term Global Income. (ooo) Formerly Van Eck World Income A.

DATA: MORNINGSTAR INC., CHICAGO

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AARP Investment Program	222-2282	MA	Liberty Financial Funds	872-5426	MA
ABT Family of Funds	553-7838	FL	Limited Term Tax-Exempt Bond Amer	See American Funds Group	
AIM Family of Funds	347-1919	TX	Lord Abbett Family of Funds	874-3733	NY
Advantage Funds	241-2039	CT	MFS Family of Funds	637-2929	MA
Alliance Capital Group	227-4618	NJ	Mackenzie/Ivy Group of Funds	456-5111	FL
American Capital Group	421-5666	TX	MainStay Funds	522-4202	
American Funds Group	421-4120	CA	Marshall Funds	236-8560	WI
Aquila Group	872-5859	NY	Merrill Lynch Group	637-3863	NJ
Asset Management Fund (AMF)	527-3713	IL	MetLife-State Street Group	882-3302	MA
Atlas Funds	933-2852		Nationwide Funds	848-0920	OH
Babson Fund Group	422-2766	MO	Neuberger & Berman Group	877-9700	NY
Baird Mutual Funds	792-2473	WI	New England Fund Group	225-7670	MA
Benham Group	331-8331	CA	Nicholas Group		WI
Bernstein Sanford C. Fund		NY	Northeast Investors Group	225-6704	MA
Biltmore Funds	462-7538		Nuveen Mutual Funds	351-4100	IL
Blair William Mutual Funds	742-7272	IL	Oppenheimer Funds	525-7048	CO
Blanchard Group of Funds	922-7771	NY	Overland Express Funds	552-9612	AR
Bond Fund of America	See American Funds Group		PIMCo Advisors Funds	426-0107	CT
California Investment Trust Group	225-8778	CA	Pacific Horizon Funds	332-3863	
Calvert Group	368-2748	MD	Pacifica Funds	662-8417	NY
Capital World Bond	See American Funds Group		PaineWebber Mutual Funds	647-1568	NJ
Cardinal Group	848-7734	OH	Paragon Portfolio	777-5143	
Colonial Group	248-2828	MA	Permanent Portfolio Family of Funds	531-5142	
Columbia Funds	547-1707	OR	Phoenix Funds	243-4361	CT
Common Sense Trust	544-5445		Pierpont Funds	521-5411	
Compass Capital Group	451-8371		Pilgrim Group	334-3444	CA
Composite Group of Funds	543-8072	WA	Pioneer Group	225-6292	MA
DG Investor Series	748-8500		Piper Jaffray Group	866-7778	MN
Dean Witter Funds	869-3863	NY	Portico Funds	228-1024	WI
Delaware Group	523-4640	PA	Premier Funds	554-4611	NY
Dodge & Cox Group	621-3979	CA	Price T. Rowe Funds	638-5660	MD
Dreyfus Group	645-6561	NY	Princor Family of Mutual Funds	451-5447	IA
Dupree Mutual Funds	866-0614	KY	Prudential Mutual Funds	225-1852	
EV Marathon and Traditional funds	See Eaton Vance Group		Putnam Mutual Funds	225-1581	MA
Eaton Vance Group	225-6265	MA	RSI Retirement Trust	772-3615	
Emerald Funds	637-6336		Ranson Managed Portfolios	345-2363	KS
Empire Builder Group	845-8406	NY	Rochester Funds		NY
FPA Funds	982-4372	CA	Safeco Mutual Funds	426-6730	WA
Federated Funds	245-5040	PA	Schwab Funds	526-8600	
Fidelity Advisor Funds	522-7297	MA	Scudder Funds	225-2470	MA
Fidelity Group	544-8888		Seligman Group	221-2783	NY
First Investors Group	423-4026	NY	Seven Seas Series Fund	647-7327	MA
First Union Funds	326-3241	NC	Sierra Trust Funds	222-5852	
Fixed-Income Securities	245-5040	PA	Sit Group	332-5580	MN
Flagship Funds	227-4648	OH	Smith Barney Funds	451-2010	NY
Fortis Funds	800-2638	MN	Smith Breeden Family of Funds	221-3138	NC
Fortress Investment Funds	245-5051	PA	Stagecoach Funds	222-8222	
Franklin Group of Funds	342-5236	CA	State Street Research Group	882-3302	MA
Fund for U.S. Government Secs A	See Liberty Family of Funds		SteinRoe Mutual Funds	338-2550	IL
Fundamental Family of Funds	322-6864	NY	Strong Funds	368-3863	WI
G.T. Global Group of Funds	824-1580	CA	SunAmerica Funds	858-8850	NY
General CA Municipal Bond	See Dreyfus Group		TCW/DW Funds		NY
General Municipal Bond	See Dreyfus Group		Tax-Exempt Bond Fund of America	See American Funds Group	
General NY Municipal Bond	See Dreyfus Group		Tax-Free Fund of CO	See Aquila Group	
Goldman Sachs Asset Mgmt Group	762-5035		Tax-Free Trust of AZ	See Aquila Group	
Gradison-McDonald Mutual Funds	869-5999	OH	Tax-Free Trust of OR	See Aquila Group	
Hancock John Funds	225-5291		Templeton Group	292-9293	FL
Harbor Funds	422-1050	OH	Thornburg Funds	847-0200	NM
Hawaiian Tax-Free	See Aquila Group		Twentieth Century Family of Funds	345-2021	MO
Heartland Funds	432-7856	WI	U.S. Government Securities	See American Funds Group	
IDS Group	328-8300	MN	USAA Group	382-8722	
ISI Funds	955-7175	NY	UST Master Funds	233-1136	MA
Intermediate Bond Fund America	See American Funds Group		United Group	366-5465	KS
International Income A	See Liberty Family of Funds		Value Line Mutual Funds	223-0818	NY
Invesco Family of Funds	525-8085	CO	Van Eck Funds	544-4653	NY
Investors Trust	656-6626	WA	Van Kampen Merritt Family of Funds	225-2222	IL
Ivy Bond A	See Mackenzie/Ivy Group of Funds		Vanguard Group	662-7447	
Janus Group	525-8983		Venture Advisers Funds	279-0279	NM
Kemper Funds	621-1048	IL	Victory Group	539-3863	
Keystone America Family of Funds	343-2898	MA	Voyageur Funds	553-2143	MN
Keystone Group	343-2898	MA	WPG Mutual Funds	223-3332	NY
Legg Mason Family of Funds	822-5544	MD	Warburg Pincus Funds	257-5614	NY
Lexington Group	526-0057	NJ	Woodward Funds	688-3350	MI
Liberty Family of Funds	245-5051	PA			

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EDITED BY AMY DUNKIN

B-SCHOOLS: DON'T OVERLOOK THESE UP-AND-COMERS

When Carlos Barrionuevo picked an MBA program, he had some very specific standards. He wanted to find a quality school with a strong finance department, a close-knit community, and a large international population. For those reasons, he passed up a chance to attend Indiana University, a BUSINESS WEEK Top 20 B-school, and chose the University of Rochester's William E. Simon School instead.

He has no regrets. In fact, the second-year MBA candidate has gotten more out of Simon than he bargained for. Thanks to an innovative program, Barrionuevo and 13

other students got the chance to shape and manage a portion of the program. "The nice thing about a small school is that you have the opportunity to make a difference," he says.

There are plenty of other reasons applicants might want to look beyond the Top 20. As part of the recently published *Business Week Guide to*

the Best Business Schools (McGraw-Hill, \$14.95), the magazine compiled a list of 20 runners-up to its 1994 Top 20 list (BW—Oct. 24). This next-best bunch, which is not ranked, was based on a survey of leading corporate recruiters. You can also find significant information on each of these schools on

BUSINESS WEEK Online, which is available to subscribers of the America Online network.

Entry to the up-and-comers as a group is likely to be easier than in the top tier. The average Graduate Management Admission Test score for these schools is 604, compared with 637 for the Top 20. On average, the runners-up group

admits 44% of students who

apply, compared with 27% for the first tier.

PAYBACK. These schools have another lure: They're generally cheaper. Top 20 schools charge 7% more for tuition, on average. And if you're a high-caliber candidate, these schools are apt to be more generous with scholarships. Eager to lure top students through its doors, Washington University's Olin School

in St. Louis doles out \$1.6 million to 63% of its students. Emory University's Business School in Atlanta is wooing hopefuls with \$1.6 million in scholarships.

You are likely to receive an excellent basic business education at these schools, and, in some cases, be exposed to creative approaches to management training. Some of these schools are forging close relationships with corporations, placing a greater emphasis on aspects of management such as diversity, ethics, and communications, and beefing up global business opportunities. And some of these institutions started with the idea of being "comer schools," which are more sensitive to how customers feel about a program, and maybe that's why we're trying to

EDUCATION

A Snapshot Of The Second Tier

UNIVERSITY/ B-SCHOOL NAME (IF ANY)	CHARACTERISTICS	AVG. GMAT SCORE	APPLICANTS ACCEPTED	ANNUAL TUITION*	NO JOBS BY GRADUATION	AVG. PAID PRE-MBA
AGSIM** THUNDERBIRD	Can enter this global program in Jan., June, or Sept. Must study culture, language, and business.	570	35%	\$23,095	29.9%	\$30,080
CASE WESTERN RESERVE WEATHERHEAD	Each MBA receives customized education. New course taps diverse group of executives.	591	51	17,600	14.0	48,170
EMORY GOIZUETA	Renamed B-school for Coca-Cola's CEO. Undergrad business majors can earn MBA in three semesters.	625	36	18,850	16.4	37,840
GEORGETOWN	This young program is carving a niche in global management and business-government relations.	619	40	19,584	12.2	36,750
MICHIGAN STATE BROAD	New dean in new building is using scholarships to attract quality students.	590†	37	16,057	6.9	29,930
PENN STATE SMEAL	Newly revised program allows greater flexibility. Boasts expertise in business-to-business marketing.	58†	19	11,400	22.5	32,470
SMU COX	Innovative program features student assessments, consulting for nonprofits, and executive mentors.	60†	55	18,034	15.5	34,880
TULANE FREEMAN	Interviews all domestic applicants. MBAs from 24 different countries graduated last year.	600	58	19,550	18.6	28,870
UNIV. OF ILLINOIS AT URBANA-CHAMPAIGN	Will launch a more practical curriculum this fall. Boasts first-rate accounting program.	616	62	12,628	22.5	27,620
UNIV. OF IOWA	Moved into new \$36 million building. 45% of MBAs come from the state. You can design your major.	590	36	9,361	13.6	22,050

*For out-of-state residents

**American Graduate School of International Management

†BUSINESS WEEK estimate

top tier," says
ph Westerfield,
USC's Graduate
of Business in
geles.

B-schools at
n Methodist
ity in Dallas and
estern Reserve
ity in Cleveland
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of the most in-
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individual needs.

A group of
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developing a series
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" skills, and attract-
porate participants.
mittee works exten-
with Citicorp, Proc-
amble, Reebok, and
other corporate spon-
re students have be-



SMU'S COX SCHOOL: *One of the most innovative MBA programs*

come partners and equity
holders in their education,"
says Charles Plosser, dean of
Rochester's B-school. "It has
also provided them with valu-
able management experience
and corporate contacts."

Another good reason to at-
tend a runners-up is the
school's close ties to the com-

munity—which come in
handy if you want to live and
work in that region. Many
have carved out niches that
are linked to their location
or draw on strengths of other
parts of the university. If
you know you want to work
in the entertainment indus-
try, for instance, consider

USC's B-school. It re-
cently developed an
"entertainment manage-
ment concentration"
that capitalizes on its
proximity to Holly-
wood—by bringing in
industry executives—as
well as the strength of
USC's School of Cinema
Television. The B-school
also boasts one of the
premier entrepreneur-
ship programs in the
country.

Corporate recruiters
consider the American
Graduate School of
International Manage-
ment in Glendale, Ariz.,
a leader in global busi-
ness. While Thunder-
bird has focused on this
for close to 50 years,
many other B-schools
are adding internation-
al content to their pro-
grams. At Washington's

Georgetown University, each
course, whether it's account-
ing, marketing, or produc-
tion, is taught from a global
perspective. As the world-
wide business community be-
comes more intertwined, in-
ternational perspective will
be a staple of B-school edu-
cation.

Lori Bongiorno

ANY)	CHARACTERISTICS	AVG. GMAT SCORE	APPLICANTS ACCEPTED	ANNUAL TUITION*	NO JOBS BY GRADUATION	AVG. PAY, PRE-MBA	AVG. PAY, POST-MBA
MINNESOTA	Boasts close ties with thriving Twin Cities business community through field projects and mentoring.	600	48%	\$12,618	9.8%	\$30,800	\$48,250
NOTRE DAME	Plans to open \$22 million building. Loyal alums aid in job search. Emphasis on ethics.	578	63	17,430	14.9	33,660	49,230
PENNSYLVANIA	Offers top-quality MBA in unique, recently revised 11-month program that allows more choices.	603	47	22,734	16.9	37,450	46,070
UTAH	Small intimate environment with large international population. Exceptionally strong finance faculty.	612	38	19,080	21.0	35,760	60,670
VIRGINIA	Top-notch entrepreneurship program. New entertainment major. Stellar organizational behavior faculty.	610	33	17,230	14.8	37,020	52,030
WASHINGTON	Seattle location helps draw quality students and faculty. Offers environmental management program.	617	42	11,436	16.7	34,610	44,140
WISCONSIN	MBAs can obtain specialized degrees in logistics, real estate, and manufacturing systems.	603	50	12,505	18.5	34,030	49,700
	Boasts extensive menu of customer service and quality courses. 10-to-1 student-faculty ratio.	610	48	19,851	12.3	33,430	54,310
YALE UNIV.	Innovative elective pairs MBAs with companies that pay for advice. Students can work with nonprofits.	608	48	18,350	11.1	31,190	53,400
	Curriculum focuses on public- and private-sector management. Draws exceptional students.	656	36	20,990	4.2	33,510	74,030

DATA: BUSINESS WEEK, BUSINESS SCHOOLS

STYLE AND COMFORT—IN A FAMILY WAY

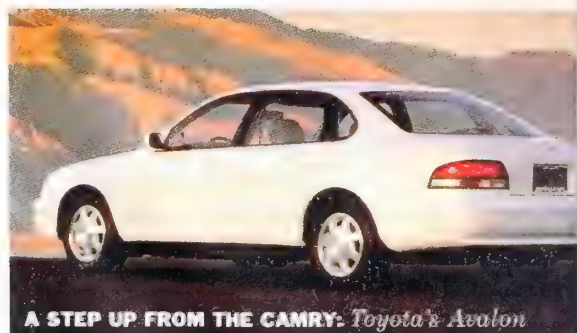
Finally, there's a big, affordable Japanese car. Toyota has taken its benchmark Camry, stretched it and plumped it, and called it Avalon. This is a car for American families, with generous legroom, a gigantic trunk, and a front bench seat—it seats six, a first for Japanese cars. Specifically, it's designed for aging baby boomers hooked on their Camrys, Honda Accords, or Nissan Maximas. Until now, the step up to a bigger Japanese car was a giant one, to a \$50,000 top-of-the-line Lexus or Infiniti. So instead, boomers defected to the likes of the Ford Taurus or Dodge

Intrepid. Now, the Avalon can be had for as little as \$22,750.

That's still a premium over American cars, but it buys you the refinement and engineering the Japanese are famous for. Everything is intuitive: Climate and radio controls are mounted high on the dash, with large, clearly marked knobs. Despite the space, nothing is a stretch or a grope.

About the only confusion: Because there's no center console, the shift lever is mounted on the steering column, alongside stalks controlling the wipers and cruise control.

The Avalon's ride is softer than the Camry's, as it should be for a larger, more



A STEP UP FROM THE CAMRY: Toyota's Avalon

luxurious car. Still, this is no American luxu-barge: It doesn't dip and sway when you're changing lanes. Even though the Avalon is slightly heavier than the Camry, it's peppier and gets better fuel economy, at 20 mpg in city driving and 28 mpg on the highway (vs. 18 and 25 for the Camry V-6).

OPTION PLAYS. The XLS model, starting at \$26,688, has all the luxury cues, including keyless entry, antilock brakes, automatic on/off climate control and headlights, and simulated wood on the

dash. Even with all the options—leather seats, compact-disk sound system, power sunroof—the won't top \$30,000. That's more than Toyota's smaller, level Lexus ES 300.

If there is anything like, it's the bland, mouse styling; the car is cult to pick out in a parking lot. At this stage in its lives, though, many buyers are looking for substance over style. And that's the Avalon, the quintessential American car, from Japanese. *Larry Aronson*

AUTOS

SMART MONEY

HOW TO PICK UP SEXIER CDs

Most people looking for certificates of deposit automatically

think of going to a bank or a savings institution. But some securities brokers can often get you more favorable rates.

Large brokerage houses such as Smith Barney, Dean Witter, Merrill Lynch, and Oppenheimer cut their own deals with banks nationwide to get better yields than those offered to individuals. "Brokered CDs tend to be significantly higher than the national averages," says Norbert Mehl, president of BanxQuotes Money Markets

in Milburn, N.J., which tracks CD rates. Just compare the 5.9% average for one-year bank CDs with the 6.68% for one-year brokered CDs. If that's too long to tie up your funds, try three months at 5.82% vs. 4.2% for banks. Like bank CDs, brokered CDs are backed by the Federal Deposit Insurance Corp. for up to \$100,000.

PAPERWORK. Where's the catch? There really is none. You don't pay any fees because the banks pay the broker commissions. The banks offer the higher yields because the brokers buy in huge quantities and take over the administration of the CDs. "We do all the paperwork, so we're saving them the cost of that overhead," says Clint Gilbert, director of the retail-CD funding desk at Smith Barney. You can keep tabs on the top-yielding offerings

by calling BanxQuote (800 666-2000) or looking up its results Wednesdays in *The Wall Street Journal*.

Brokered CDs got a bad name during the 1980s, when ailing thrifts were offering particularly high rates. When some of the CD

risk-averse customers pined and to lure new clients in the hopes of selling more lucrative products, wouldn't say the consumer can't do any better on her own," says Gail Lerman, editor of *The Bank Rate Monitor*. Indeed,

individual banks offer even better yields. Imperial Thrift in Glendale, Calif. (800 927-2000) and Midwest Savings in Columbus, Ohio (800 686-2052), the brokers with month CDs at 6.5% and 6.5%, and one-year CDs at 7.11

Best Bets With Brokered CDs

BROKER	3 MO.*	6 MO.*	1 YR.*	MIN.
DEAN WITTER	5.65%	6.0%	6.45%	\$1,000
MERRILL LYNCH	5.82	6.21	6.54	1,000
OPPENHEIMER	NA	6.09	NA	5,000
SMITH BARNEY	5.7	6.0	6.5	1,000
BANK AVERAGE	4.2	4.89	5.9	VARIOUS

* YIELD AS OF 1/30/95 DATA: BUSINESS WEEK NA=NOT AVAILABLE

issuers failed, customers forfeited the juicy returns, even though deposit insurance protected their principal. Now, the FDIC only allows registered brokers to buy CDs from the most highly capitalized banks.

Brokerages promote high-rate CDs to keep their

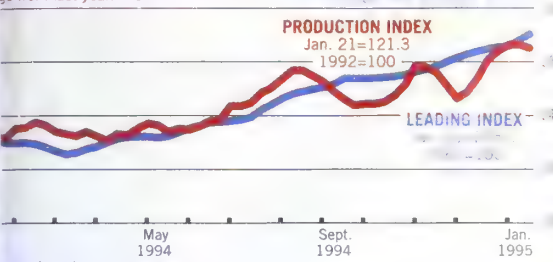
and 7%, respectively.

But it may be inconvenient to deal with a far bank. And some of the bank rates aren't available to out-of-state consumers. So you might want to get the absolute highest rate for the ease of calling a broker. *Pam Blum*

Business Week Index

PRODUCTION AND LEADING INDEXES

Change from last week: -0.3%
Change from last year: 7.3%



The production index fell slightly during the week ended Jan. 21. But before the four-week moving average, the index increased to 121.9, up 1.4. Higher lumber and coal production lifted the index. The leading index posted a solid increase in the latest week. The unaveraged so gained ground, reflecting higher stock prices, fewer large-business failures and a faster growth rate in M2.

Production index copyright 1994 by McGraw-Hill Inc. BW leading index copyright 1994 by CIBCR.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
PRICES (1/27) S&P 500	467.56	468.18	-1.4
LATE BOND YIELD, Aaa (1/27)	8.49%	8.44%	22.9
MINERAL MATERIALS PRICES (1/27)	114.5	114.0	NA*
SS FAILURES (1/20)	266	299	-8.9
STATE LOANS (1/18) billions	\$463.3	\$462.4r	10.5
SUPPLY, M2 (1/16) billions	\$3,580.8	\$3,572.7r	1.4
CLAIMS, UNEMPLOYMENT (1/14) thous.	325	354	-11.0

*Center for International Business Cycle Research (CIBCR). Standard & Poor's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures companies), Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on failures and real estate loans. *Historical data available from CIBCR.

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
FEDERAL FUNDS (2/1)	6.00%	5.45%	3.17%
DISCOUNT RATE (1/31) 3-month	6.24	6.26	3.20
LIBOR (1/27) 3-month	6.23	6.27	3.20
LIBOR (1/27) 30-year	9.32	9.25	7.08
LIBOR (1/27) one-year	6.83	6.90	4.22
LIBOR (2/1)	9.00	8.50	6.00

Source: Federal Reserve, HSH Associates, Reuters Holdings PLC

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (1/28) thous. of net tons	2,001	1,991#	12.4
AUTOS (1/28) units	132,344	113,310r#	-12.8
TRUCKS (1/28) units	114,965	91,028r#	-9.9
ELECTRIC POWER (1/28) millions of kilowatt-hrs.	62,932	59,187#	3.2
CRUDE-OIL REFINING (1/28) thous. of bbl./day	13,404	13,553#	
COAL (1/21) thous. of net tons	21,939#	21,731	42.4
PAPERBOARD (1/21) thous. of tons	NA	NA	NA
PAPER (1/21) thous. of tons	NA	NA	NA
LUMBER (1/21) millions of ft.	479.6#	464.6	1.7
RAIL FREIGHT (1/21) billions of ton-miles	24.0#	24.2	32.6

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPAA¹, SFPA², Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (2/1) \$/troy oz.	376.250	381.450	-1.3
STEEL SCRAP (1/31) #1 heavy, \$/ton	147.00	147.00	5.4
COPPER (1/28) \$/lb.	146.0	145.5	61.7
ALUMINUM (1/28) \$/lb.	104.0	100.5	79.3
COTTON (1/28) strict low middling 1-1/16 in., \$/lb.	89.29	88.44	28.7
OIL (1/31) \$/bbl.	18.46	18.66	15.0

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (2/1)	99.46	99.71	108.44
GERMAN MARK (2/1)	1.52	1.52	1.74
BRITISH POUND (2/1)	1.58	1.59	1.49
FRENCH FRANC (2/1)	5.28	5.26	5.91
ITALIAN LIRA (2/1)	1609.0	1599.0	1690.5
CANADIAN DOLLAR (2/1)	1.41	1.42	1.33
MEXICAN PESO (2/1) ³	5.500	5.755	3.103

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

THE WEEK AHEAD

ACTIVITY & COSTS

Feb. 7, 10 a.m. ▶ Output per worker in the nonfarm sector probably edged up or fell slightly in the fourth quarter. Although economic output seems to have grown robustly, so did total hours worked, as indicated by surging job growth over the workweek. The expected uptick at yearend means that productivity rose about 2% in 1994 after a 1.5% increase in 1993. In the factory sector, productivity is still going strong, with a gain of about 1.5%, at an annual rate in the fourth quarter. In the third quarter, nonfarm productivity grew 3.1%, manufacturing increasing 3.5%. Unit costs in the nonfarm sector probably

rose at an annual rate of about 3% last quarter, after no change in the third period, but factory unit costs most likely slid for the fifth consecutive quarter. The slack showing of productivity at the end of 1994 will rev up the debate over the structural upturn in productivity in the U.S.

INSTALLMENT CREDIT

Tuesday, Feb. 7 ▶ Consumers probably added about \$10.5 billion in new debt in December, according to the median forecast of economists surveyed by MMS International, a division of McGraw-Hill Inc. The expected increase would be a bit below the \$11.6 billion in October and \$12.9 billion in November. The hefty accumulation of

new borrowing suggests that the holiday shopping season was significantly financed by credit cards.

PRODUCER PRICE INDEX

Friday, Feb. 10, 8:30 a.m. ▶ Producer prices of finished goods probably increased by 0.4% in January, says the MMS forecast. Most likely, suppliers used the first of the year to pass along price markups. Excluding food and energy, core prices likely also increased by 0.4% in January. In December, both the total PPI and the core index edged up only 0.2%. However, the Labor Dept. is scheduled to release new seasonal factors to the PPI data that may change the December increases.

*in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense
1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

U.S. Savings Bonds Are Now Tax Free For College. Good News Today. Better News In 18 Years.



If the cost of a college education seems expensive now, imagine what it will be in 18 years. That's why Bonds bought for your child's education can be completely tax free. Start buying Bonds today at your local bank, or ask about the Payroll Savings Plan at work.

U.S. Savings Bonds



The Great American Investment

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Index to Companies

This index gives the starting page for a story or feature with a significant reference to a company. Most subsidiaries are indexed under their own names. Companies listed only in tables are not included.

A

Advanced Micro Devices **64**
Alliance North American Government Income Fund **94**
Alliant Techsystems **80**
American Capital Tax-Exempt High-Yield Municipal **94**
American Cyanamid **88**
America Online **8, 22, 90, 91, 112**
America West **6**
Ames Department Stores **64**
Amgen **88**
Apple Computer **22, 90, 91**
Aprax **80**
AT&T **50, 64, 90, 91**
Avid Technology **22**

B

Banamex **36**
Bancomer **36**
Bank of Tokyo **56**
BanxQuotes Money Markets **114**
BASF **54**
Bear Stearns **74**
BellSouth **22, 54, 64**
Ben & Jerry's **50**
Blockbuster Videos **8**
Boise Cascade **48**
Bristol-Myers Squibb **88**
British Petroleum **74**
Brod Capital Management **88**
Burda **91**

C

Cable & Wireless **54**
Capital Cities/ABC **48**
Cargill Investor Services **62**
Centerton Nursery **10**
Cheung Kong Holdings **60**
Chevron **74**
Chiat/Day **50**
Chiron **88**
Chrysler **64, 72**
Ciba-Geigy **88**
Citicorp **112**
CompuServe **90, 91**
Continental Airlines **64**
Continental Bank **88**
Crédit Lyonnais **60**
CS First Boston **56, 84**

D

De Beers **76**
Dean Witter **114**
Deutsche Telekom **54**
Dow Chemical **80**
DuPont **53, 80**

E

Eastman Kodak **50**
Emerging Markets Franchise Acceleration Fund **8**
Empresas ICA **36**
E-Plus Mobilfunk **54**
Europe Online **91**
Exxon **6, 28**

F

Fidelity Aggressive Tax-Free Portfolio Fund **94**
Fidelity Asset Manager Fund **46**
Fidelity Investments **38, 46**
Fidelity Mortgage Securities Fund **94**
Fidelity Short-Term Bond Fund **46**
Fidelity Spartan Short-Term Income Fund **46**
Financial Research **94**
First Mississippi **48**
Ford **36, 40, 64, 72, 112**
Forrester Research **90**
FPA New Income Fund **94**
France Telecom **54, 91**

G

Gaines Berland **74**
Gallatin Steel **64**
GE **48, 50, 64, 76**
Gerber Products **88**
Getty Petroleum **74**
GM **40, 64**
Goldman Sachs **28**
Greyhound **6**
GTECH **88**

H

Heinz (H.J.) **88**
Hewlett-Packard **64, 67**
Hoechst **50**
Home Depot **64, 65**
Honda **114**

I

IBM **64, 90**
Imperial Thrift **114**
Industrial Bank of Japan **56**
Info-Prod **61**
Insignia Systems **22**
Intel **64**
Internacional de Cerámica **36**
International Game Technology **88**
Intuit **64**
Iridium **54**
Italia Online **91**

J

Johnson & Johnson **64, 80**
Jostens **48**
Jupiter Communications **90**

K

Kemper **84**
Kemper Financial Services **36**

Kentucky Fried Chicken **8**

Kmart **48**

KPMG Peat Marwick **28**

L

L.A. Gear **50**
Lehman Brothers **74, 88**

M

Marion Merrell Dow **50**
Matra-Hachette **91**
McCaw Cellular Communications **64**
McDonald's **8**
McGraw-Hill **115**
McKesson **88**
Medley **94**
Melville **48**
Mercer Management Consulting **64**
Merrill Lynch **86, 114**
Microsoft **22, 64, 90, 91**
Midland Realty International **60**
Midwest Savings **114**
Minitel **91**
Mitsubishi Bank **56**
MMS International **115**
Morgan Stanley **55, 86**
Morningstar **46, 94, 96**
Morris Air **64**
Motorola **22, 64**

N

Nabisco **8**
NatWest Securities **64**
Navistar International **48**
NBC **48, 60**
New York Life **80**
New York Muni Fund **94**
Nextel Communications **64**
Nielsen Media Research **48**
Nintendo **50**
Nissan **36, 114**
Novel **22**
Nucor **64, 70**
Nynex **90**

O

Olivetti **91**
Omnicon **50**
Omron **13**
Oppenheimer **114**
Oryx Energy **48**

P

Pacific Telesis **64**
PaineWebber **40, 94**
PaineWebber Short-Term U.S. Government Income Fund **94**
Pearson **91**
Pennzoil **74**
PepsiCo **8**
Pet **88**
Pfizer **80**
Phoenix Information Systems **13**
Pizza Hut **8**
Porsche **55**
Procter & Gamble **80, 112**
Prodigy **90, 91**

R

Reebok **112**
Rely **22**
Ryka **50**

S

Salomon Brothers **56, 72**
Samsung Electronics **36**
Santa Fe Pacific
Sears **64, 90**
Serfin **36**
Siemens **55**
Sitrick **6**
Smith Barney **1**
Smith Breiden
Duration U.S. Government Fu
Sony Electronic
México **36**
Southern New E
Telephone **64**
Southwest Airlin
69
Sprint **54**
Stac Electronics
Standard & Pool
Strong Advantag
Fund **94**
Sullivan & Crom
Sumitomo **56, 7**

T

Taco Bell **8**
TBWA **50**
Tenneco **50**
Texaco **74**
Thyssen **54**
Tiger Asset
Management **4**
Time Warner **64**
Toyota **114**

U

Unilever **88**
United Airlines
U.S. Healthcare
U.S. Shoe **48**
U.S. Steel Group

V

Vanguard Fixed-
Short Term Cor
Bond Fund **94**
Vanguard Group
Veba **54**
Venture Muni (+
B **94**
VF **64**
Viag **54**
Vistek Electronic
VLSI Technology
Volkswagen **36,**

W

Wal-Mart **64**
Walt Disney **8**
Weil, Gotshal &
Manges **86**
Wertheim Schroe
WordPerfect **22**
Wyatt **28**

Z

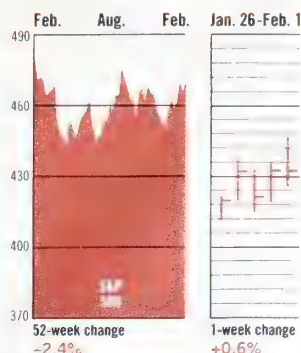
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Zurn Industries

Investment Figures of the Week

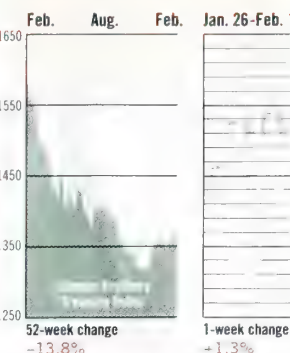
TARY

Markets were buoyed by Clinton's bold step to aid the peso, which surged 15% and nearly 10% on Jan. 31, strength spreading quickly to Mexican and Asian markets, which had been rallying last week, took a hit on the Fed hiked short rate. U.S. stocks continue to range. But the technicians shown on this page are higher. Gold mining is the exception, as gold prices are in the doldrums.

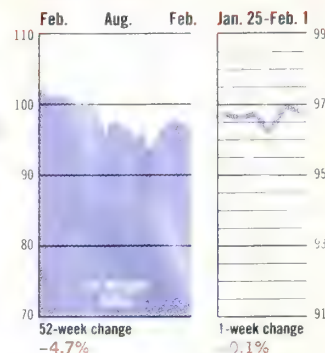
STOCKS



BONDS



THE DOLLAR



STOCK ANALYSIS

STOCKS	Latest	% change	
		Week	52-week
INDUSTRIALS	3847.6	-0.6	-3.2
COMPANIES (S&P MidCap Index)	171.7	0.1	-6.7
COMPANIES (Russell 2000)	247.5	-0.5	-7.5
COMPANIES (Russell 3000)	269.0	0.6	-3.4

STOCKS	Latest	% change (local currency)	
		Week	52-week
FINANCIAL TIMES 100	3017.3	1.2	-14.3
NIKKEI INDEX	18,739.5	3.2	-7.5
DAX COMPOSITE	4019.1	-2.1	-12.1

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	6.05%	5.93%	3.13%
30-YEAR TREASURY BOND YIELD	7.74%	7.86%	6.28%
S&P 500 DIVIDEND YIELD	2.75%	2.77%	2.43%
S&P 500 PRICE/EARNINGS RATIO	16.1	16.6	22.6

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 200-day moving average	459.0	458.4	Positive
Stocks above 200-day moving average	40.0%	38.0%	Positive
Speculative sentiment: Put/call ratio	0.64	0.68	Neutral
Insider sentiment: Vickers sell/buy ratio	0.87	0.88	Positive

BLOOMBERG FINANCIAL MARKETS

STOCK GROUPS

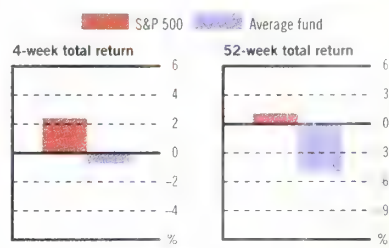
STOCK LEADERS	% change		Strongest stock in group	% change		Price
	4-week	52-week		4-week	52-week	
PHARMACEUTICALS	10.8	4.1	WENDY'S INTERNATIONAL	12.2	-8.5	16 1/8
HEALTH CARE SERVICES	9.5	-6.2	ALZA	30.6	-13.4	23 1/2
MANAGEMENT	9.0	1.0	COMMUNITY PSYCHIATRIC CENTERS	11.4	-29.0	12 1/4
INVESTMENT	9.0	0.8	VIACOM	13.2	28.1	46 1/8
TELECOMMUNICATIONS	8.9	-27.5	USAIR GROUP	23.5	-63.5	5 1/4

STOCK LAGGARDS	% change		Weakest stock in group	% change		Price
	4-week	52-week		4-week	52-week	
MINING	-11.5	-28.2	SANTA FE PACIFIC GOLD	-22.1	NA	10 1/8
TELECOMMUNICATIONS	-10.6	-26.1	ROADWAY SERVICES	-11.9	-27.8	50
TELECOMMUNICATIONS	-9.1	-18.2	INLAND STEEL INDUSTRIES	-19.6	-19.6	28 1/4
TELECOMMUNICATIONS	-8.8	-30.7	FORD MOTOR	-9.4	-24.6	25 1/4
TELECOMMUNICATIONS	-7.9	-4.4	PHELPS DODGE	-15.4	-1.6	52 3/8

MUTUAL FUNDS

total return	%	LAGGARDS	Four-week total return	%
OPPORTUNITY	8.3	WRIGHT EQUIFUND-MEXICO NATL. FID. EQTY.	-27.3	
ARNEY TELECOMM. INCOME	7.7	UNITED SERVICES GOLD	-23.4	
ARNEY TELECOMM. INCOME	7.3	BULL & BEAR GOLD INVESTORS	-19.3	

total return	%	52-week total return	%
FINANCIAL COMMUNICATIONS & INFORM. A	24.7	MONITREND GOLD	-55.5
SELECT HEALTH CARE	24.2	STEADMAN OCEANOGRAPHIC TECHNOLOGY	-42.9
TECHNOLOGY A	23.5	STEADMAN AMERICAN INDUSTRY	-40.2



RELATIVE PORTFOLIOS

Units represent the value of \$10,000 one year ago	Money market fund	Foreign stocks	U.S. stocks	Gold	Treasury bonds
Relative returns	\$10,493 +0.27%	\$10,452 +1.98%	\$10,094 +0.98%	\$9,650 -1.68%	\$8,866 +2.59%

This page is as of market close Wednesday, Feb. 1, 1995, unless otherwise indicated. Outposts include S&P 500 companies only; performance and share prices are as of market close Jan. 31.

Mutual fund returns are as of Jan. 27. Relative portfolios are valued as of Jan. 31. A more detailed explanation of this page is available on request. r=revised NA=Not available

LESSONS FROM THE PESO SCARE

It was a financial Desert Storm. A multinational bailout force, marshaled by the U.S. and armed with \$52.8 billion, rode to the rescue of Mexico's economy. It was close, but with the stabilization of the peso and the sharp snapback of foreign stock markets, the world has now weathered its first liquidity crisis in securitized capital. Never before had a crisis occurred in a global financial system where individually owned mutual funds, not banks, played so significant a role in financing emerging countries. Never before had the world's top multilateral financial institutions, the International Monetary Fund, and the Bank for International Settlements, played the savior in this strange new land of people's capitalism.

Two lessons emerge. First, Congress, political animal that it is, refuses to be a lender of last resort to the global financial system. Partisan politics and a parochial viewpoint prevented the legislative branch from shouldering international obligations in a crisis. It is now clear that however legitimate populist issues may be at home, the parochialism that fuels them has no place in international financial affairs. In the end, it fell to the tried-and-true, politically insulated, international monetary institutions to do the job. The IMF and the BIS

gave more than half the resources—in effect, providing cover for the U.S. Treasury to play its role.

One can only ask why this obvious solution to the Mexican peso crisis was not set in motion on Jan. 1 instead of Jan. 2. Had steps been taken earlier, the world would not have brought to the brink of financial meltdown. Bumbling magnitude hasn't been seen since the savings-and-loan

The second lesson is that a multilateral safety net is more important in a world where markets, rather than banks, provide the bulk of international financing. Markets are more sensitive to risk, and they reacted more quickly than banks when they lent in the 1970s. Banks didn't mark their loans to market when OPEC devastated the world. Mutual funds do, and the risk is visible every morning. If they are to continue investing in Latin America and other individuals, like the banks before them, require a lender of last resort. The world financial system was far closer to the edge in January than most people in Congress chose to realize. Mexico needed help. If help hadn't materialized, a liquidity crisis would certainly have followed—and with it a sharp slowdown in world economic growth.

PUTTING BALANCE IN A BALANCED BUDGET

Stop me before I spend again!" Sadly, the proposed balanced-budget amendment is nothing more than a plea by our nation's political representatives to save them from themselves and their addiction to government spending. At worst, it is an exercise in hypocrisy by people who already know what to do to cut the federal deficit but lack the political courage to do it. At best, the balanced-budget amendment will provide political cover for Congress to do the right thing and cap entitlement spending. Mangling the Constitution, however, is a pretty high price to pay for financial sobriety.

Yet it may be inevitable. Polls show that the American public overwhelmingly favors a balanced-budget amendment. But while people want to cut the deficit and slash taxes, they don't want cutbacks in government programs that benefit them. This public schizophrenia has paralyzed Washington for decades. Hence the call for a binding mechanism in the Constitution that substitutes external discipline for internal will in order to kick the national spending habit. In a society where millions are "in recovery" for all kinds of addictions, the balanced-budget amendment is nothing less than a national 12-step program. Alas, we have come to this.

If America must have a balanced-budget amendment, three caveats are essential for it to have any chance of working. First, enabling legislation that contains exceptions for economic emergencies, such as severe recessions, must be written. What happens, for example, if there is a bad recession in 1996 and the deficit jumps temporarily to \$300 billion? Must

Congress then be forced to raise taxes, deflating an already weak economy and making the recession much worse?

Second, states that must balance their budgets are also committed to borrow money for building roads and bridges. A federal balanced-budget amendment demands a new, separate capital budget that lets Washington borrow for long-term improvements in the nation's infrastructure—from highways to information superhighways.

Third, paying for a balanced budget must be done fairly and equitably. Democrats dissemble when they say that Medicare, Medicaid, and Social Security, the largest of entitlement programs, are off the table. Republican hints that some entitlements may be included are not sufficient. There simply can be no balanced budget without cutting them. Fortunately, the pain need not be as severe as many fear. Shifting people out of Medicare and Medicaid and into maintenance organizations and preferred-provider organizations could save almost \$400 billion over seven years, or 30% of all the savings needed to balance the budget.

The best that can be said for the balanced-budget amendment is that it creates an opportunity to rethink government. Companies that reengineer themselves generate more productivity and profits than those that blindly hack away. Now is the time for Americans and their representatives to stop whining about taxes and benefits and make hard choices about the core functions of government. Pity they don't have the true grit to do it without debasing the Constitution.

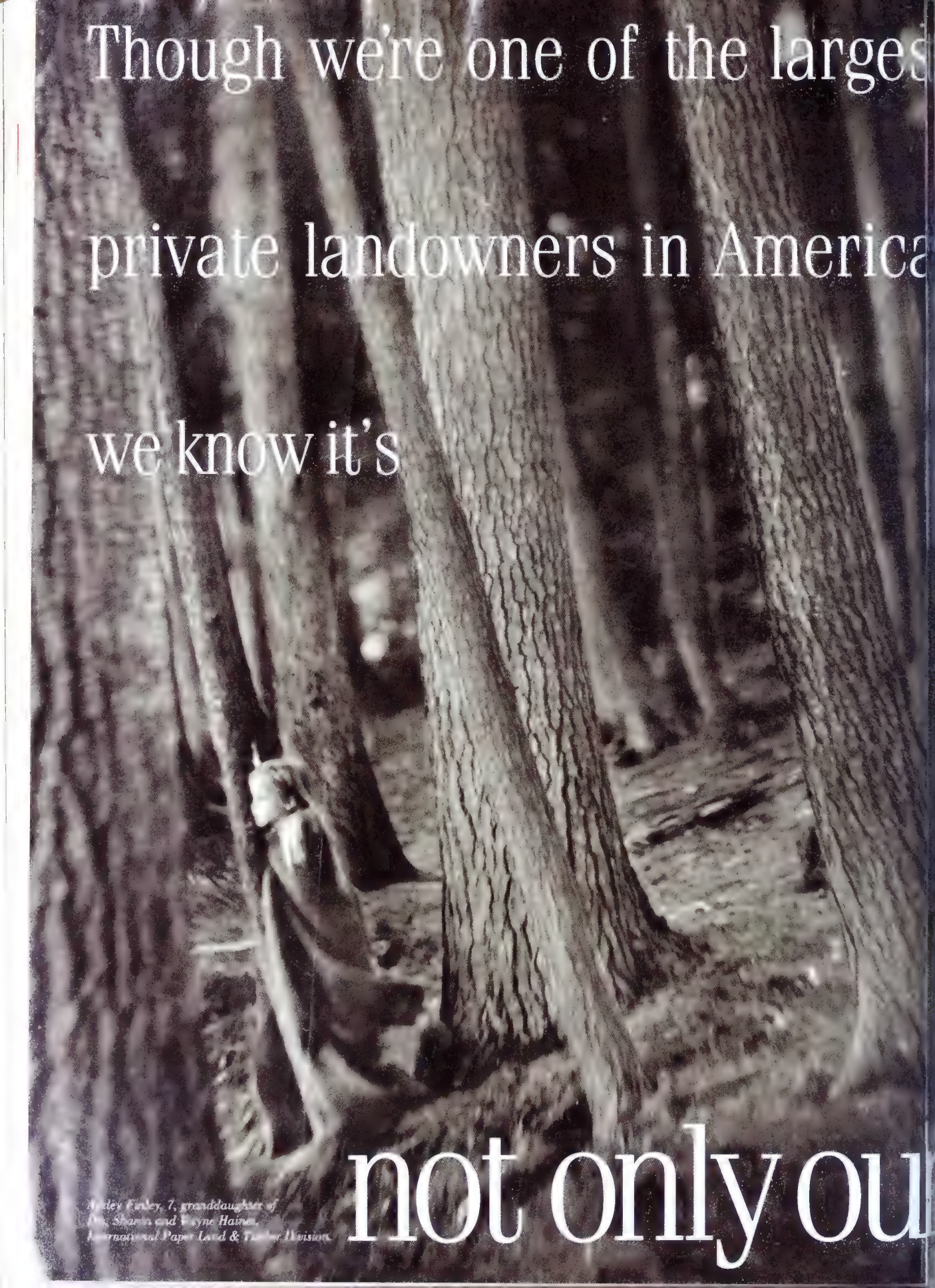
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it was Kiev. Now they're
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private landowners in America
we know it's

not only our

*Riley Farley, 7, granddaughter of
Mr. Shorn and Wayne Haines,
International Paper Land & Timber Division*

5 WEEK
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Power Macintosh

A man in a grey suit, white shirt, and red patterned tie, wearing glasses, is crouching in a dark, ornate room. He is looking directly at the camera with a slight smile. His hands are resting on the floor. In the background, there is a wooden door, a small television set on a shelf displaying a landscape image, and a large wooden chair. The lighting is dramatic, with the man's face and suit highlighted against the dark background.

Matt Ghourdjian
National Director of Technology
Howrey & Simon

With offices in Los Angeles and Washington, D.C., Howrey & Simon is considered one of the most technologically savvy law firms in the nation. "It's great," says Matt. "When the senior partner has a Power Macintosh 8100 with two 21" monitors, you know there's not much resistance to new technology."

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federation.”

If there's one thing that the world will never run short of it's business advisers.

They're queuing up to offer their personal, and all very different, prescriptions to ease your business ills. There is, however, one thing on which they all seem to agree.

The traditional, lumbering, top-heavy and multi-layered corporations of today cannot survive in the new chaotic marketplace.

And what do they predict in their place? Federations of smaller companies and groups free to move quickly and efficiently in an ever changing marketplace.

Are they right? Can a Federation really work? At Cable & Wireless we have to answer in unequivocal "yes" to both questions.

We've been operating as a Federation for some time and we're now the fifth largest telecommunications group in the world.

It's a position we've attained by steadily building up partnerships with over fifty individual groups, including over a dozen Governments, twenty local companies and more than twenty five other communications operators worldwide.

And when we say "partnerships" we mean it. If the situation demands it, we're prepared to accept a minority share.

After all, it allows the 40,000 people who work with us to select ideas, experience, equipment and even skilled personnel from a worldwide menu.

Take the mobile network set up recently by our colleagues at MTN in South Africa.

Because of their partnership with Cable & Wireless they were able to trawl the Federation for systems, equipment, advice and even key personnel.

They took a billing system, sales and marketing experience, and technical support from our partners in the UK (Mercury) and Bahrain (Batelco).

In fact they had so much support from the Federation that they were able to get the network running in a record five months.

That's how the Federation has worked for us. Over the next few weeks we'll be showing how it could work for you.

It's worth a read. After all, your business life might just depend on it.



THE CABLE & WIRELESS FEDERATION

An alliance of the world's most creative communications companies.

BusinessWeek

FEBRUARY 20, 1995

COVER STORY

A wave of criticism is rising against the sales practices and lush incentives at some of Wall Street's most prestigious brokerages—and regulators are joining in

ARTHUR LEVITT JR.
SECURITIES & EXCHANGE COMMISSION

Cover Story

70 CAN YOU TRUST YOUR BROKER?

With commission pay creating intense pressure to generate sales, particularly of house-brand funds, critics say firms are putting their own interests ahead of customers'. And unless the industry responds, it may slip into a slow decline

72 ARTHUR LEVITT'S MISSION

The SEC chairman is behind investors

74 SHOOTING STRAIGHT AND CASHING IN

Why clients gave kudos to John Olson

75 DEFENDING AN EMBATTLED INDUSTRY

PaineWebber President Joe Grano Jr.

76 "I WAS RIPE FOR PICKING"

An investor gets taken to the cleaners

News: Analysis & Commentary

32 THE CHINA TRADE

Even if the current impasse is settled, U.S.-China trade relations could be headed for continued trouble

34 COMMENTARY

The budget: Clinton has made plenty of cuts, but he shouldn't leave the radical surgery up to the GOP

35 LETTER FROM WASHINGTON

Sick of high taxes and higher crime rates, the middle class is fleeing the capital in droves

36 BIG BLUE'S WHITE ELEPHANT

Selling its not-so-high-tech Armonk headquarters is likely to take some time. And those orange carpets!

37 DIVIDING TIME WARNER

A plan to fix the balance sheet by isolating cable assets is super-vexed

38 CHILD CARE 'R' NOT US

A study says most of it is mediocre. Can Corporate America help?

40 UNITED'S "DUMB" IDEA

Its California Shuttle is winning fans and putting Southwest on notice

44 GENERAL MAGIC'S SPELL

After the Apple spin-off's much-awaited IPO, investors will really have to wait

44 SGI VS. MICROSOFT

Silicon Graphics makes two animation acquisitions—and turns up the heat

48 IN BUSINESS THIS WEEK

Robert Haft, nickel, Orange County offer, peace for Michigan National, pet food, Blockbuster-IBM, Saab-GM

International Business

54 MEXICO

Developer Paul Reichmann tries comeback in Mexico City—only the peso's collapse slam his project

55 COMMENTARY

What the IMF needs is a first-rate system

56 GERMANY

Suddenly, Germans love to hate banks—and that could presage an era of corporate control

60 RUSSIA

Impatient investors are staging shareholders' revolt that may oust the corporate old guard

61 INTERNATIONAL OUTLOOK

Mexican President Zedillo's push for democratic reform could set off explosion—especially in his own country

Economic Analysis

22 ECONOMIC VIEWPOINT

Kuttner: Social Security will run only if wage growth doesn't improve. And that's a big if



VIDEO WARFARE

Suddenly, the videodisk standard Toshiba and Time Warner are pushing looks like the one to beat

page 64



TELEPHONE FRENZY

Consumers are pouring in as deregulation technology reshape telecommunications



BEYOND PENTIUM

Intel's new chip, the P6, is ready to go. But is the market ready to buy?

page 88

WHO'LL BLINK?

Clinton is hanging tough on China—and business is with him

page 32



STAYING HEALTHY AFTER 40



It's time to treat your body right. A special Personal Business guide to health care and fitness for baby boomers

page 98

ECONOMIC TRENDS

America's trade ace in the hole, fixing oversized morale, the "old old" get on; Germany is a contender again

BUSINESS OUTLOOK

In spite of January's weak employment numbers, the economy is still running better than the Fed would like

Government

WASHINGTON OUTLOOK

Is Gephardt isn't running for president. Well, not exactly

Tele Corporation

WHY TOSHIBA TOOK TINSELTOWN

In spite of stiff odds, the videodisk standard it developed with Time Warner is picking up big backers

IT SO SWEET TIMES AT HONEYWELL

After a decade in the dumps, the company may find itself on the block

Legal Affairs

WHY DELTA'S BIG WIN

Beleaguered Pan Am by using all the tricks in the book—and then some

Mutual Fund Scoreboard

78 OPEN SEASON FOR BOTTOM-FISHERS

Many closed-end funds are bruised but beckoning to bargain hunters

Science & Technology

88 INTEL KEEPS MOVING FASTER

The chipmaker is already working on the successor to the Pentium's successor

89 NEXGEN: BEARDING A GIANT

Intel can't afford to ignore the upstart

91 DEVELOPMENTS TO WATCH

Lasers for satellites, how braids toughen composites, cleaning up with horseradish, bone-loss detector

Special Report

92 GRABBING THE TELECOM RING

Say good-bye to the trusty old phone company—nowadays, just about anybody can start one

97 THE NEW ERA BEGINS IN ROCHESTER

It's the first city to deregulate its local phone markets

For information on reprints of this Special Report, call Business Week Reprints at 609 426-5494, or write Business Week Reprints, P.O. Box 457, Hightstown, N.J. 08520.

Personal Business

98 HEALTH AFTER 40

A special section on midlife care: Exercise routines for boomer bodies, the blood test for prostate cancer, and medicine by modem

Features

6 UP FRONT

16 READERS REPORT

16 CORRECTIONS AND CLARIFICATIONS

17 BOOKS

Baldwin: *Edison: Inventing the Century*

20 TECHNOLOGY & YOU

Plug-and-play is only \$50 away—if corporate buyers would only ask for it

86 INSIDE WALL STREET

Love triangle at Abbey Healthcare
Whitman may have three easy pieces
Too quick on the trigger?

107 BUSINESS WEEK INDEX

108 INDEX TO COMPANIES

109 INVESTMENT FIGURES OF THE WEEK

110 EDITORIALS

Don't let China off the hook
Brokers should heed the wake-up call

Up Front

EDITED BY LARRY LIGHT WITH RUTH COXETER

COUNTING BEANS

SALOMON'S CREATIVE WRITE-OFF COURSE

SALOMON INC. blames a bookkeeping screw-up for helping to produce its record 1994 net loss of \$364 million. But details on how that happened are, well, skimpy.

Sanford C. Bernstein & Co. analyst Guy Moszkowski, however, fleshes out how embarrassingly lax Salomon's financial controls have been. A big boo-boo: Salomon's London office



SALOMON TRADERS: Pound foolish?

tracked assets in local currencies while recording liabilities in dollars. As the value of the greenback steadily declined in recent years, liabil-

TALK SHOW "I'm not sure Congress is the right place to organize the national pastime."

—House Speaker Newt Gingrich on whether Congress might force ballplayers and owners into binding arbitration

ities were reported in slowly shrinking dollar values, asset gains in rising local currencies. Both gains and losses should have been recorded in local currencies, Moszkowski says. The company says it fixed the problem, and Moszkowski believes the snafu won't be repeated.

Salomon says bookkeeping errors produced a huge charge that, on an aftertax basis, amounted to more than one-third of the 1994 loss. Trading setbacks, which hit the securities industry across the board, were the other large weakness.

Salomon says layoffs are next. "We are reviewing all business lines with the intent of reducing head count," says a spokesman for the firm. *Elizabeth Lesly*

BUDGET FUSSING

TEETERING SUPPORT FOR AN AMENDMENT

THE BALANCED BUDGET amendment, a key piece of the GOP agenda, seems set to death in the Senate, despite large public support and speedy House approval. One backer, Senator J. Bennett Johnston (D-La.), admits the Constitutional amendment needs two to three votes short of the 67 needed to O.K. it, and momentum is with opponents.

Senate nose counterweights that to him when the amendment comes up in late February. The amendment needs two Democratic votes, but one-time port of call: John Breaux (D-La.) and Byron Dorgan (D-N.D.). Breaux, spooked by a recent Treasury study saying budget cuts would devastate his home state, now calls the amendment "fraudulent" and says he "may quite well" oppose it. Senate Republicans, who hold 53 of the chamber's 100 seats, are unlikely to persuade maverick Appropriations Committee Chairman Mark Hatfield (R-Ore.), the lone Republican holdout.

The amendment could still be salvaged by a compromise. Senate Majority Leader J. Dole (R-Kan.) could win over more Democrats by exempting Social Security from cuts. And there's a long-shot plan to inspire grass-roots pressure on undecided Democratic senators who vote against the amendment next year and are up for reelection in 1996. Among the targets: Joseph Biden of Delaware, Max Baucus of Montana, and Tom Harkin of Iowa. *Richard S. Dunham*



BREAUX: Off the bus

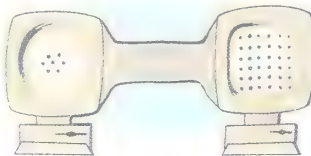
I-WAY PATROL

WIRING THE NET FOR GABFESTS

INTERNET PHONE CALLS ARE the newest lane on the Infobahn. Cheaper than regular phone service, too. And this is no illegal hacker invasion of phone-company circuits. VocalTec in Northvale, N.J., plans to storm the net on Feb. 13 with a \$49 piece of software that lets PC owners chat over a microphone with others who are similarly equipped. The only charge is the ordinary Internet access fee, around \$15 a month, with no limit on the number or length of calls.

VocalTec's Israel-based engineers stand a good chance of setting key technical standards for what experts believe will be an explosion of Internet voice service over the next few years.

Don't rush to sell your AT&T stock just yet. VocalChat works and sounds more like citizens band radio. Only one person can speak at a time, and you can't chat with



people outside the Internet itself. Moreover, you get an annoying delay of a second or two on each side of a VocalChat conversation. Sound

When the Baby Boomers hit the retirement rolls, everybody knows that fewer working folks will be around to

support them than there are now. The situation, though, is far worse in other industrialized nations. In America, the labor-force population at least will grow; in other major nations, it will shrink. By 2040 in the U.S., that translates to 3 workers for every retiree



PENSION PAYERS

quality is rough, yet quite acceptable.

The market for this? Specialty niches where a true phone call would be costly and a low-quality connection is just fine: People playing games, parents talking to children at college, maybe engineers collaborating. International callers could save big money, too. *John W. Verity*

THE LIST SUPPORTING THE AGED

(down from 5 to 1 now). In Germany in 2040, that's 2 workers per retiree (down from 4.5 to 1 today). Birthrates have been falling all over the developed world, but in America the lower birthrate is offset in part by higher levels of immigration.

LABOR FORCE GROWTH BY 2040*

1. U.S.	18%
2. BRITAIN	-5
3. JAPAN	-19
4. ITALY	-22
5. GERMANY	-41

*Cumulative projected growth of population, age 15-64 DATA: U.N.

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CAPITAL OFFENSES

A FEE FOR LENDING UNCLE SAM MONEY?

THE DAYS OF PURCHASING Treasury securities directly from the government for free may be numbered. In May, the feds will assess a \$25 fee on all Treasury Direct accounts of \$100,000 or more. Sure, \$25 is a pittance for

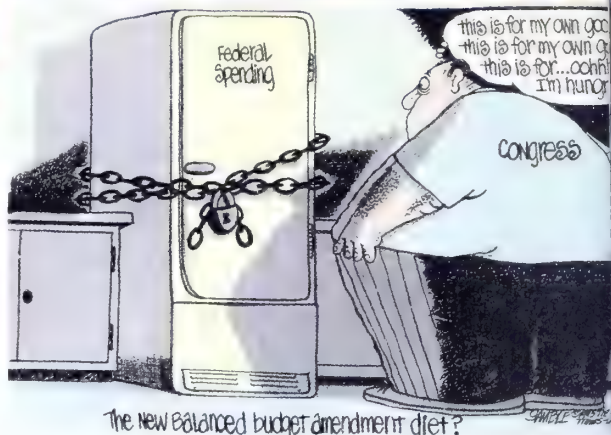
enables people to bypass brokers, who charge commissions of \$50 or more per transaction. The \$25 Treasury Direct maintenance fee is a bid to recoup some of the program's \$25 million annual cost, although the \$2.5 million expected in its first year isn't much.

To fixed-income sages such as Jay Chitnis, a bond dealer with Stoeber Glass in New York, the fee on heavyweight investors could be "a revenue-raising trial balloon." John Markese, president of the American Association of Individual Investors,

expects that fees on \$10,000 accounts may not be far off. Then, people may simply go to brokers, he says.

Meanwhile, the U.S. Bureau of the Public Debt swears that there are no plans afoot to extend the fees. Still, concedes spokesman Peter Hollenbach, "anything's possible." *Amey Stone*

DRAWN & QUARTERED



PAPER PLAYS

A LOW GRADE FOR THIS BOND GRADER

YOU JUST DON'T UNDERSTAND. That's what companies sometimes say to the people who rate their bonds. But the folks at the National Association of Insurance Commissioners, who rate private-placement debt, are really under fire. This debt is purchased, usually by an insurer, directly from the issuer rather than in the open market.

The snag is that the NAIC—unlike big-time debt raters such as Moody's—hasn't been using industry specialists for its ratings (which run from NAIC-1 at the top, down to NAIC-6). The NAIC method: Ratings analysts divvy up the

companies alphabetically rather than by industry.

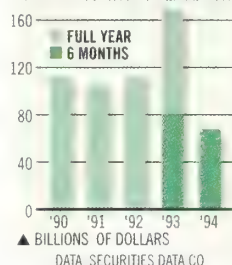
So HCI USA Distributors squawked that the analyzing companies began with the letter "H" made a bad call when it gave a NAIC-3 rating for its million private placement lot is at stake: The high rating, the lower the company's interest tab.

the U.S. subsidiary of Hollander Chemical, last got upgraded to NAIC-2.

The NAIC says it is remedying this by moving to an industry-based system and doubling the size of its rating staff, to 23. Says

spokesman Ed Barks: "This is an evolutionary process. The staff may get a breath." The spiraling private-placement volume is off late thanks to higher rates.

NEW ISSUES OF NONCONVERTIBLE DEBT VIA PRIVATE PLACEMENT



FEDERAL PAPER: An IOU with attitude

someone able to spring for a hundred grand's worth of T-bills. But some bond experts think fees will next be imposed on the common folk who hold far smaller amounts for their accounts, where the Treasury keeps their paper, as a brokerage does.

The Treasury Direct program, in operation since 1986,

SLUGFESTS

CORPORATE CREDOS: VOWS THAT AREN'T

MAYBE CORPORATE CREDOS don't mean much after all—legally anyway. A U.S. District Court judge just ruled against a former employee who said Johnson & Johnson violated its corporate mission statement by firing him in 1989. In his wrongful termination

suit, former R&D executive Daniel Tripodi pointed to a line in the credo that says workers "must have a sense of security" (Up Front, Nov. 21). And that, argued Tripodi, is a binding contract. The 51-year-old credo lays out the company's responsibilities to customers, employees, and others.

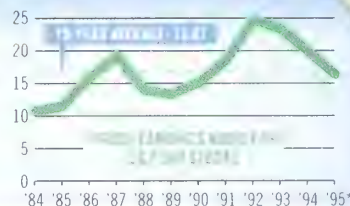
In December, a jury sided with Tripodi and awarded him \$434,000. But Judge Dickinson Debevoise set

aside the verdict. He said the credo lists "general policies or goals" and is "aspirational rather than contractual." Tripodi's lawyer is planning to appeal, although the odds of gaining a reversal are slim. *Joseph Weber*

THE BIG PICTURE

MORE FOR YOUR MONEY ON WALL STREET

Stocks are a better value these days, as measured by their price-earnings ratio—stock prices divided by earnings over the past year. In 1994, prices wobbled around but ended about where they started. Meanwhile, partly because of corporate belt-tightening, profits zoomed.



DATA: STANDARD & POOR'S CORP

*AS OF JAN. 31

FOOTNOTES

The average cost increase for a medical plan in 1991: **14%**. In 1994: **2%**

One play can mean the difference between winning and losing. One fax can mean the difference between the right play and the wrong one. Perched high in a press box at Soldier Field with a bird's eye view of the opposing defense, Chicago Bears offensive coordinators diagram plays and send them down to the sideline. They send them down to a Muratec plain-paper fax with superfine resolution and image smoothing. After all, a picture can be worth more than a thousand words. Six points to be exact. Muratec. 1-800-543-4636



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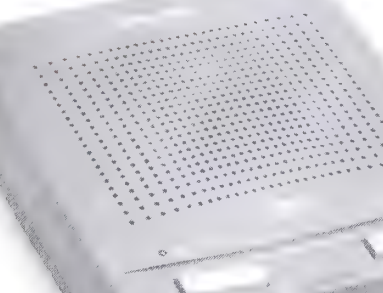


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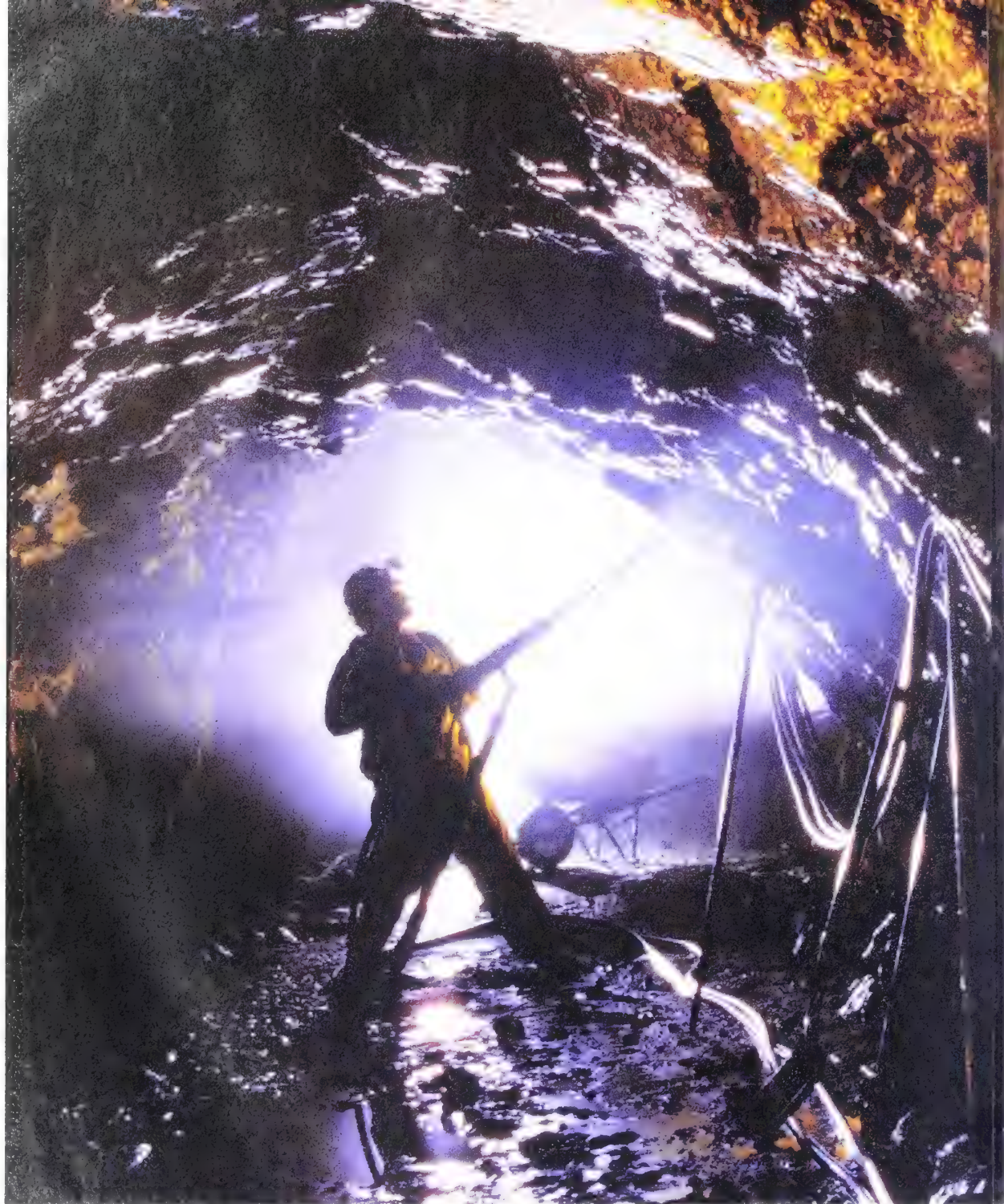
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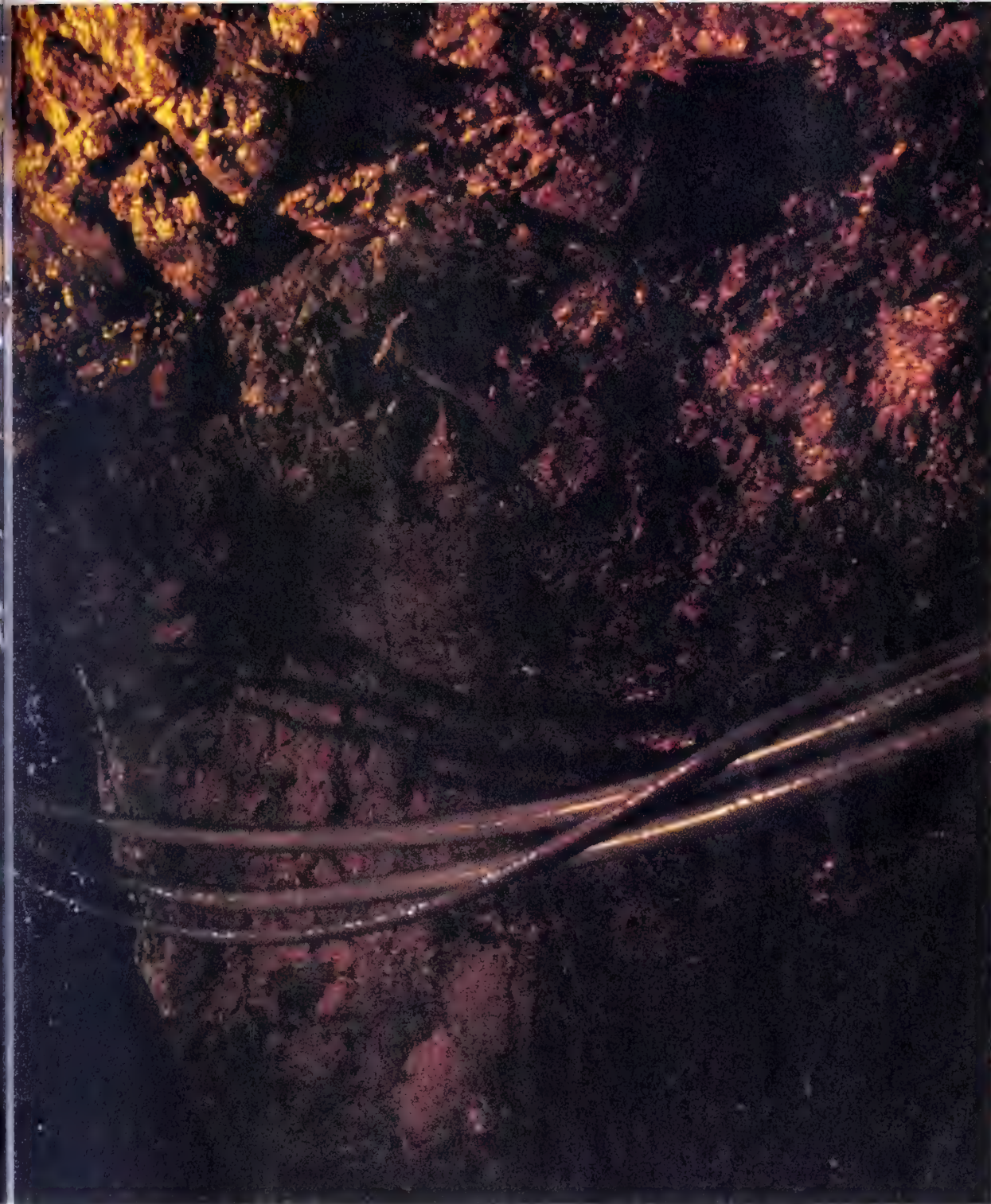


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HOW TO CUT THE HIGH COST OF TAXES

In "Simplifying taxes would save a bundle" (Editorials, Jan. 30), you ignored the issue of state taxes. The federal tax form is difficult but doable by the average citizen. Many people have to fill out multiple convoluted state tax forms with radically different sets of rules and intricacies.

The solution would be to have the federal government collect all taxes and redistribute the money to the states and cities. The only outstanding issue would be finding jobs for all the ex-state tax workers and accountants.

David Weil
Bergenfield, N.J.

Your editorial is right on the mark. The estimated \$75 billion cost of tax compliance is unproductive waste which could be better applied in more productive endeavors.

James I. Morgan
Midland, Mich.

GIVE THE HOME LOAN BANKS SOME CREDIT

Your article "Riskier and riskier at the home loan banks" (Finance, Jan. 30) incorrectly characterized the Federal Home Loan Bank System. The truth is, Standard & Poor's gives the banks a AAA rating, its highest. Why? Because of our high level of capitalization, low interest-rate risk, negligible credit risk, strong liquidity, and sound management.

We are proud of our contribution to affordable housing in communities across America, and we look forward to serving our important mission in the years to come.

Michael A. Jessee
President and Chief Executive
Federal Home Loan Bank of Boston

A CALL FOR TOUGH LOVE IN MEXICO

I have read several articles on Mexico and the measures that the U.S. and several countries are going to take to

CORRECTIONS & CLARIFICATIONS

"Making your long-distance dollar go the distance" (Personal Business, Jan. 30) stated that consumers subscribing to MCI's Friends & Family program get a 30% discount when they make \$75 or more a month in long-distance calls. In fact, the 30% discount kicks in at the \$50 level.

In the Mutual Fund Scoreboard for bond funds (Feb. 13), the boxes were inadvertently omitted from the explanation for "Trend" on page 97. ■ for the top quartile; ■ for the second quartile; ■ for the third quartile; and □ for the bottom quartile.

Also, in "Bond funds: Nowhere to go but up?" (Feb. 13), the sales charge on the FPA New Income Fund should have been 4.5%.

"B-schools: Don't overlook these up-and-comers" (Personal Business, Feb. 13) incorrectly stated estimates of the Graduate Management Admission Test Scores for Pennsylvania State University's Smeal College of Business Administration and Southern Methodist University's Edwin L. Cox School of Business. BUSINESS WEEK estimates that Penn State's average GMAT score is 580 and SMU's is 600.

"Fidelity's new contract with America" (News: Analysis & Commentary, Feb. 13) should not have said that Fidelity Investments' shift in investment strategy was preceded by Thomas J. Steffanci's "ouster." As the story said, Steffanci resigned from his post.

help Mexico ("Washington to the rescue. Now, about the price..." International Business, Jan. 30). My response is: Do not lend any more money to this damned country.

The only people who benefit are the politicians like Salinas, who privatized several very important state companies and became one of the richest men in the world. He lied to all of us citizens of Mexico, saying that everything was O.K.

Yes, everything was O.K. for him. However, he led the country to become

nearly bankrupt and transformed more than half of the population into street vendors.

Paolo Sagh
Cuernavaca, Mexico

BIG LONG-DISTANCE DISCOUNTS TAKE THE RIGHT CONNECTIONS

Your article "Making your long-distance dollar go the distance" (Personal Business, Jan. 30) was accurate in limited extent.

You failed to mention where the savings can be achieved. Long-distance resellers utilize their volume purchasing to offer significant discounts we compared to dealing direct with the major carriers. Savings of 30% to 50% are not uncommon.

James A. We
Min

REVIEWING PILGRIM'S PROGRESS

We take strong exception to F. Schine's characterization of the performance of our funds in 1994, as reported in "Is Pilgrim making any progress?" (Finance, Jan. 30).

Despite a very difficult stock market and the worst bond market in recent history, Pilgrim's funds outperformed the 25 largest stock funds and are now up 15 of the past 16 years. Pilgrim High-Yield Trust was ranked 18th out of 93 high-yield funds by Lipper Analytical Services Corp.

Pilgrim Prime Rate Trust, our closest fund that invests in senior, collateralized floating-rate bank loans, was ranked No. 1 in its category by Lipper for the one- and five-year periods ended Dec. 31, 1994.

While it is true that our adjustable rate mortgage (ARM) funds, like many other ARM funds, had poor performance in 1994, it is also true that our ARM funds were the top performers from 1991 to 1993.

Jeffrey S. Llo
Vice-President for Markets
Pilgrim Group
Los Angeles

LETTERS FOR READERS REPORT

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 Neil Baldwin
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EDISON: WHAT MADE THE LIGHTBULBS GO ON?

Thomas Alva Edison was wrong—egregiously and lastingly wrong—so often that it seems as though rigid adherence to error was an undeniable byproduct of his way of thinking. He was wrong about electricity, in on transmitting by direct current after George Westinghouse's alternating-current networks had carried the day. He was wrong about the phonograph, favoring his original cylinder recordings over platters. He spent a dusty decade on a quixotic crusade to extract iron from crushed rocks with magnets. Late in life, he refused to use radios, calling them "radio" and a "craze."

Neil Baldwin's excellent biography, *Edison: Inventing the Century*, dives deeply into the thought processes of this operating genius, showing how the stubbornness that led to his failures also contributed to his epic successes. Although Edison's inventions ranged from infrared photography to making rubber from gold, he was no dabbler: His favorite method for solving a problem was to try everything. In the search for a light-bulb filament, for instance, he and one of his lieutenants, Charles Batchelor, medically tested dozens of carbonized materials, including celluloid, cedar, cotton hair, fish line, and, finally, cotton thread.

Although he had only a grade-school education, Edison was endlessly sure of himself. This confidence enabled him to test fledgling notions or prototypes—aided by a series of well-chosen assistants—turn them into fully functioning products and systems. The light-bulb. The carbon-button transmitter that

improved Alexander Graham Bell's telephone. The phonograph. The motion picture. Even a better kiln for making Portland cement—not glamorous, but one of Edison's most profitably sustained inventions.

Baldwin is too nuanced a writer to attribute all of Edison's achievements to his thick stubborn streak. As he shows, Edison had a restless mind that tended to cast all experience into the framework of problems in need of solving. He couldn't watch the waves during a sea voyage without wondering how to harness their energy. And he was able to perceive fresh connections—as when he figured out that the gear from his failed iron ore separation project could be applied to his work in cement. Writes Baldwin: "Edison's ideas never seemed to die, but coexisted in tandem for decades, transmuting, growing, held in abeyance until the right moment for exploitation when a synapse fired and they became manifest."

Certainly he was no 1990s-style CEO. He never evinced much interest in profit. Although rich, he railed against wealth and declared that "interest is an invention of Satan." He disdained corporate life: After being named a director of General Electric Co. at the inaugural board meeting in 1892, he never attended another meeting. What's more, he was given to public musings about the supernatural. It's hard to imagine GE's Jack Welch speculating about human intelligence becoming affixed to things in nature, such as trees.

For all that, Edison was a powerful force for modernization. What set him

apart from his inventive peers was his lifelong interest in building systems, not just devices. Electric lighting is the classic example. Not content with making a bulb, Edison built an entire infrastructure. Edison Electric Light Co., a predecessor of GE, manufactured and installed everything required to illuminate the night—from the bulbs to the huge coal-fired generators known as dynamos.

Baldwin describes this organic thinking as "refreshingly modern." It's no surprise that Henry Ford, the perfecter of the assembly line, was Edison's camping partner and greatest admirer. Baldwin, who has written biographies of the artist Man Ray and the poet William Carlos Williams, is especially strong in situating Edison in the intellectual context of his times. Henry Adams, he says, was thinking of masterful men such as Edison and Ford when he wrote that "the new American... must be a sort of God compared with any former creation of nature."

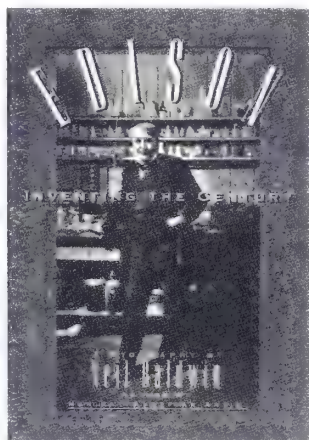
Of course, the "Napoleon of Invention," as the press dubbed him, also had a private life. And Edison the man was as maddening as Edison the inventor. He worked so late—frequently around the clock—that his three eldest children wound up starved for love. Widowed at 37, he later married a beautiful heiress and had three more children. But he continued his workaholic ways, jotting notes to his wife from a northern New Jersey iron mine, complaining about the malfunctioning ore elevator and wheeling: "I do not see why you can't stay for a week at a time."

Edison never eased up because he was convinced it was work, not braininess, that brought him success—hence his famous assertion that "genius is 1% inspiration, 99% perspiration." The single most important quality for an executive, he contended, was "a fine memory." To Edison, Baldwin writes, memory "was the cornerstone for the ability to make a quick, correct decision, marshaling all the facts at one's disposal."

In an era when how-to titles on management and creativity seem to flood into bookstores, readers in search of inspiration could do worse than to read this richly detailed biography of the greatest inventor in American history.

BY PETER COY

Coy covers technology for BUSINESS WEEK.



THE GREAT INVENTOR'S FAVORITE METHOD FOR SOLVING A PROBLEM WAS TO TRY EVERYTHING

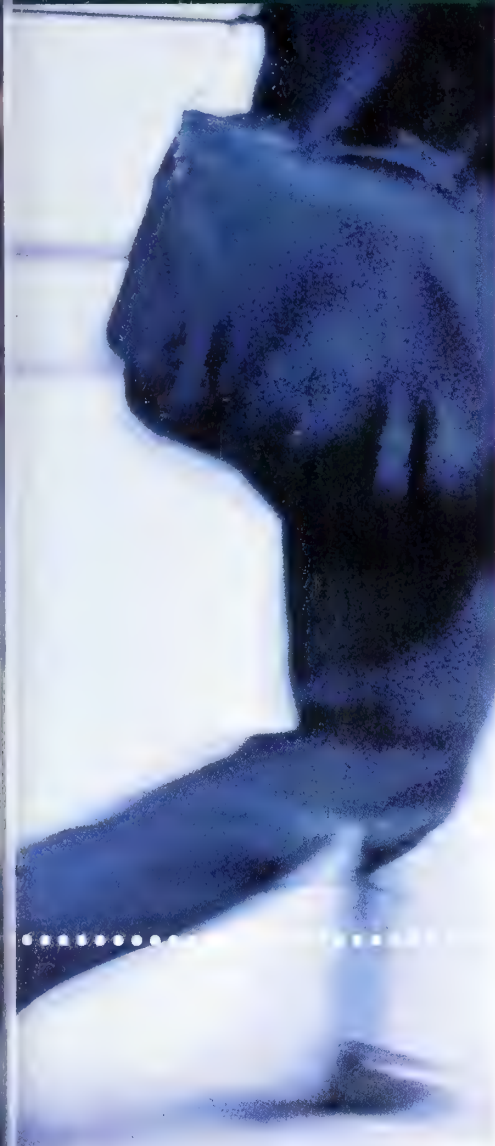


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EDITED BY STEPHEN H. WILDSTROM

PLUG-AND-PLAY IS ONLY \$50 AWAY

I have a lot of experience adding accessories to PCs, and I've gotten pretty good at it. Still, I approach each job with trepidation. The physical chore of installation is pretty simple—a couple of screws, a cable or two. But getting everything to work together is another story. Depressingly, this problem could be greatly eased at a cost of about \$50 per computer, but the economics of corporate PC purchases get in the way.

A couple of weeks ago, I discussed the incompatibilities between multimedia applications and video systems that drive home-PC owners nuts (BW—Feb. 6). In the office, the culprit is more likely the demands put on your Windows or DOS computer by a local-area network.

TRIAL AND ERROR. A case in point was my recent test of an Okidata Doc-It combination laser printer-fax-scanner. When I set it up, I discovered that I could either use the Doc-It or log on to our network. It took a couple of hours of trial-and-error frustration before I could do both. This is a shame. The \$1,500 Doc-It is a capable machine that would be an asset to many business users, but they may find it just too hard to install.

The nastiest configuration problems, like those besetting the Doc-It, involve networks and a type of interface called small computer

system interface (SCSI) (pronounced "scuzzy") that's used with CD-ROM drives, scanners, and other devices requiring high-speed communications. The problem is a legacy of PC design, which has remained basically unchanged since IBM introduced the PC AT in 1984. All add-on devices demand computer resources—these are the things that show up as "IRQs" and "I/O addresses" in configuration



menus—from a very limited pool. Two devices wanting the same resource behave like two 3-year-olds wanting the same toy.

Network and SCSI interfaces can sort out conflicting demands—as they do on the Macintosh. Connect an Ethernet cable, and your Mac is on the network. Plug in a scanner or a new disk drive, and you're ready to roll. In fact, you can hang up to seven devices on a single, built-in SCSI interface.

Don't hold your breath waiting for personal-computer makers to emulate Apple Computer Inc. Built-in networking and SCSI connections are found on some high-end PCs, especially those intended

for use as network file servers. Hewlett-Packard Co.'s NetServer is an example. But it's a different story on most machines destined for the business desktop.

It turns out that it would add no more than about \$25 to the retail price of a machine to add SCSI and another \$25 to build in networking on your personal computer. But computer makers say even such a minuscule premium would leave them at a competitive disadvantage in the marketplace. "With a lot of corporate customers, it's not unusual for \$25 to be the deciding factor," says Andrew Watson, Compaq Computer Corp.'s director of marketing for desktop products.

MYOPIC MISTAKE. This is shortsighted for big corporations, which probably spend many times that \$50 solving problems for users, and tough on smaller businesses that lack in-house support.

Some help may be on the way. Watson expects at least built-in networking to become widespread in the next year or so, mainly because it's

now cheaper for a buyer to get an interface built in rather than add on a networking card. But unless standard SCSI support is added, too, the struggle will continue.

A bigger assist would come if Microsoft's oft-delayed Windows 95, now scheduled to hit the market in August, lives up to its promise of plug-and-play installation of accessories. But so far, full plug-and-play compatibility has proven elusive.

This is one personal-computer problem that buyers, at least the big corporate ones, have the power to solve. Manufacturers will give customers what they want. But first, those customers have to ask.

BULLETIN BOARD

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THE BILL GATES COLLECTION

When not busy running Microsoft, CEO Bill Gates has been snapping up electronic-distribution rights to much of the world's great art. Now you can see why. Corbis Publishing, the privately held company Gates set up to handle his



rights, has come up with its first consumer product. It's a stunner. *A Passion for Art* by Corbis (206 641-4505) is a \$45 Windows tour of the Barnes Foundation's collection of Impressionist and Post-Impressionist art. The disk offers tours narrated by art historians and the ability to browse through galleries. The program is the best proof to date that multimedia is not just for kids.

SOFTWARE

SORTING IT ALL OUT

If you're like most computer users, your hard disk has become a collection of mostly forgotten file names, and finding a letter or spreadsheet you created a few months ago is a big challenge. If you want to get organized—and are willing to put some work in the effort—OnFile from Software Publishing (800 234-2500) can be a big help.

The \$50 Windows program lets you organize your files into "books" and "chapters" rather than by file type or directory. A big plus for future retrieval: You can replace cryptic eight-letter file names with real descriptions.



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BY ROBERT KUTTNER

SOCIAL SECURITY: IF IT AIN'T BROKE, DON'T TINKER



GOOD NEWS?

The system will run dry only if the 1% wage growth of the past 20 years doesn't improve. But there's ample reason to believe it will

Social Security is supposedly in long-term demographic crisis—too many retirees living longer, not enough wage earners to pay the freight. As a result, there have been calls for reduced Social Security payouts, deferred retirements, perhaps even means-testing. But a closer look at the economic assumptions behind the Social Security Trustees' Report reveals a very different sort of crisis—one that calls for different solutions.

Social Security is financed by payroll taxes. Unless we raise tax rates, growth in payroll-tax receipts will depend on growth in taxable wages. The trustees project likely annual real wage growth of just 1% per year over the next 75 years. By contrast, during the past 75 years, annual real wage growth was about 1.7%. Because of compounding, this seemingly small difference puts the economy on a wholly divergent growth trajectory. With 1% real annual wage growth, Social Security will be hundreds of billions in the red. With 1.7% growth, the system will be in the black forever.

Why the trustees' pessimism? Wage growth has indeed been dismal during the past two decades. From 1953 to 1973, annual productivity grew by 2.3%, and wages grew annually at 2%. But in the slow-growth decades from 1973 to 1993, while annual productivity grew at just 0.9%, real wages actually declined—an average of 0.2% per year.

PRODUCTIVITY. The key question is whether coming decades will resemble the fat years or the lean ones. Here perhaps is some good news. First, 1973-93 had unusual demographic trends unlikely to be repeated. Baby boomers and women flooded into the workforce, leaving less wage per worker. Baby boomers, male and female, are now more experienced and presumably more productive workers. Women workers are now being paid wages closer to their male counterparts. On both counts, the one-time depression in wages should be reversed.

A second source of lower wages has been the galloping increase in the cost of fringe benefits. Wages are subject to Social Security taxes; benefits are not. Here again, the recent past does not predict the future. One way or another, via market forces or government regulation, the escalation in health premiums will level off. The other major fringe benefit, pensions, is already declining as a share of total compensation.

Third, many economists expect the boom in information technology to translate, at least in part, into higher productivity. Economic history suggests long lags between the introduction of new, productivity-enhancing technology and its broad economic diffusion. In addition, as Massachusetts Institute of Technology economist Frank S. Levy notes, the productivity gains of the 1950s showed up almost immediately in higher purchasing power, because they were concentrated in consumer goods. The productivity improvements of the 1980s and '90s, in contrast, have been in producer technologies. However, as computers proliferate and information technology reduces productivity gains in everything from banking and retailing to telephone services, these gains will likely yield gains in consumer wages, too.

"MORONIC." Offsetting this optimism, however, are two other factors. First, income distribution has become increasingly unequal. If that trend continues, too few of the productivity gains will show up in pay packets subject to payroll taxation. Moreover, despite the Fed's competitiveness and resulting low inflation, the Federal Reserve seems determined not to let the economy reach its full growth potential. But here the solution is not to wimp on Social Security. It is rather to pursue policies that reverse the growing income inequality and permit greater economic expansion.

Nobody, of course, can predict the ratio of wage increases 75 years into the future. But one expert working on the Social Security actuarial assumptions confesses, on deep background: "The whole exercise, really, is moronic." During the past 75 years, we experienced one entirely unanticipated wage collapse, the Great Depression; an equally unexpected stimulus to wage growth, World War II; and a third unpredicted slowdown after 1973.

In truth, even under pessimistic assumptions, Social Security will remain nicely in balance for at least the next 20 years. Whether the system goes into the red after that depends on trends nobody can forecast with certainty. Rather than hack away at Social Security, Congress should legislate standby adjustments to take effect only if the doomsayers prove right. We should continue to pursue economic expansion and rising wages—both for Social Security and in their own sakes.

Robert Kuttner is co-editor of *The American Prospect* and author of *The End of Laissez-Faire*.



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INSURANCE & INVESTMENT

BY GENE KORETZ

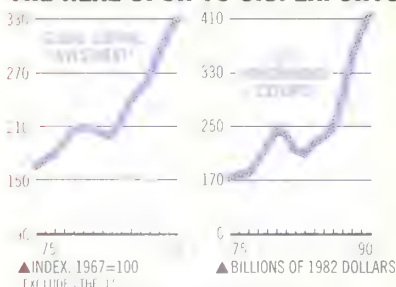
AMERICA'S TRADE ACE IN THE HOLE

Global capital spending is surging

America's spectacular export surge since the mid-1980s is usually attributed to the combined impact of the sharply declining dollar and economic growth overseas. Economist Andrew M. Warner of the Harvard Institute for International Development contends, however, that this view misses a critical determinant of U.S. export growth: capital spending in foreign economies.

In the latest issue of the *American Economic Review*, Warner analyzes the relationship of shifts in U.S. export growth to changes in foreign consumption, capital investment, and economic growth. Over the past 25 years, he finds that U.S. merchandise exports are far more closely tied to foreign investment patterns than to either foreign economic growth or consumption, particularly in the past decade. Indeed, the influence of overseas investment on U.S. export performance even overshadows the con-

THE REAL SPUR TO U.S. EXPORTS



siderable impact of dollar depreciation.

This picture parallels ongoing changes in America's industrial structure. Since 1967, the capital equipment share of U.S. manufacturing output has jumped from 28% to nearly 40%, and the percent of capital goods that is exported has climbed from 20% to 45%.

The influence of foreign investment demand on U.S. exports helps explain why they have been so variable, since investment itself is a highly variable component of economic growth. Warner's findings also imply that the role of a depreciating dollar in America's export performance has been exaggerated, while the importance of the nation's technological expertise in capital goods

areas may well be underappreciated.

In this light, U.S. efforts to shore up Mexico's economy and keep its crisis from spreading appear more than prudent. Given the developing world's investment boom and Europe's growing interest in productivity-enhancing investment, the outlook for U.S. exports seems brighter and brighter.

MORALE GOT DOWNSIZED, TOO

Can managers repair the damage?

It's no surprise that employee morale suffered in the wake of corporate restructuring. According to a recent Wyatt Co. nationwide survey of 4,300 working Americans, only 57% of workers in downsizing companies indicated they were generally satisfied with their jobs, compared to 72% of workers in expanding outfits.

The good news, however, is that employers are waking up to the problem and that the downsizing trend itself may be losing steam. Cambridge Human Resources Group Inc., a Chicago-based outplacement firm, says a survey of corporate human-resources executives reveals that "revitalizing their workforces and restructuring the workplace in downsized companies" are their top priorities in 1995. Meanwhile, *Human Resource Executive* magazine reports that the nation's top 50 employers cut their net payrolls by only 92,300 employees last year, down from a drop of 146,800 in 1993.

GERMANY IS A CONTENDER AGAIN

Productivity soars, labor costs sag

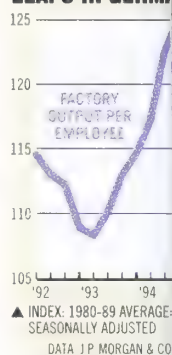
Germany is still wrestling with the burden of reunification, but there is no gainsaying the remarkable revival of West German industrial competitiveness. As economist Ralph Süppel of J.P. Morgan & Co. notes, manufacturers have successfully pushed through large-scale reforms while obtaining major concessions from labor unions on wage growth and work-time flexibility.

From its cyclical low in late 1992, Süppel reports, productivity has surged an impressive 15.5% (chart), or close to 10% after adjusting for rising utilization due to faster demand growth. That's the best two-year gain since the 1960s.

As a result of the productivity and wage growth below 1.5% last year, unit labor costs in the third quarter were down 10% from their cyclical high. The drop, the largest in postwar history, more than offset a 6% rise in the value of the trade-weighted mark.

Although higher wage gains and slower productivity growth will inevitably push unit labor costs up as the expansion matures, Süppel notes that Germany's competitiveness has already boosted its export performance and has touched off renewed domestic capital spending. That should result in employment growth and, by the end of 1995, recovery in household spending.

PRODUCTIVITY LEAPS IN GERMANY



THE 'OLD OLD' GET EVEN OLDER

The 80-plus group is growing fast

The common view is that once you're 80, you're headed downhill fast, inevitable natural aging processes kick in to bring life to an end. A study in the latest issue of *Population and Development Review*, however, suggests that longevity for those in their 80s and may, in fact, be increasing significantly—a trend with major social and economic implications.

In the study, demographers Väinö Kannisto, Jens Lauritsen, A. Ronald Thatcher, and James W. Vaupel analyzed mortality data for people in their 80s and 90s in developed countries. They found that death rates of the "old" have been declining at an accelerating pace since the 1920s, but particularly in recent decades. In a sample of countries, for example, average death rates for men and women in their 80s declined by 0.7% and 1.2% a year, respectively, from the 1960s to the 1970s, but by 1.2% and 1.9% annually in the 1980s. Indeed, in a number of nations the pace appears to have quickened even more through the early 1990s.

If such trends were to continue over coming decades, the 80-plus group in advanced countries, already the fastest rising contingent among the elderly, would far exceed current projections.

Q: As a senior manager, do you ever think about your computers' data storage?

A: No.

Q: It doesn't hold the least bit of interest for you?

A: Not really.

Q: Ever ask your MIS people to explain the latest trends in storage?

A: Never.

Q: Did you know your competitors could be using data storage to eat your lunch?

A: What? Data what?



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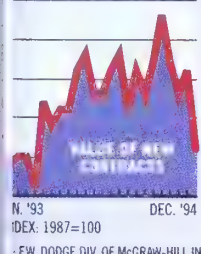
JAMES C. COOPER & KATHLEEN MADIGAN

THE ECONOMY STILL ISN'T COOL ENOUGH FOR THE FED

U.S. ECONOMY After seeing the weak numbers in January's employment report Feb. 3, people seem convinced the long-awaited economic slowdown is finally here. Even the ever-skeptical market reacted with unabashed bullishness, which pushed stocks sharply higher as well, on the belief that the Federal Reserve may be finished hiking interest rates. The Clinton Administration also has a substantial investment in the notion. The White House economic forecast accompanying its fiscal 1996 budget projects growth taper off, from 4% in 1994 to 2.4% in 1995, with only a slight pickup in consumer-price inflation, from 2.6% to 3%. More important, the Clinton team is saying that no interest rate hikes are necessary to achieve these results. Really? These folks had better take a closer look at last month's labor market data. The details of the report just don't support the surprisingly soft headline numbers. Yes, the economy is starting to cool down from its 4%-plus pace in the second half of 1994. But by how much? Most of the January data now available suggest that first-quarter growth remains on the north side of 3%, not below it as the Fed desires.

BE SURE, the first hints that past Fed tightening is beginning to hold are in the air. You can't completely dismiss January's modest 134,000 increase in company payrolls, the first in a year, or the jump in the jobless rate to 5.7% from 5.4% in December. And that moderation comes on the heels of softer-looking retail sales, three quarters of sluggish inventory growth, and weaker home buying—not to mention the largest plunge in new construction contracts in three years (chart).

NEW CONSTRUCTION TAKES A TUMBLE



The value of new building contracts dropped 8% in December, with homebuilding, business construction, and public-works projects all down. Homebuilding suffered the most, as sales of new single-family homes fell 0.6% in December, despite warm weather, and the month's supply of new homes for sale is now the highest in about four years. But so far, these straws in the wind are hardly proof of a broad slowdown, especially when other labor-market indicators show no change in their recent trends. New jobless claims at the end of January were no higher than their fourth-quarter average,

and the Conference Board's index of help-wanted ads jumped 3% in December to a 3½-year high. Both measures are dependable forward-looking gauges that suggest labor-market strength, not weakness.

The most compelling sign that the job markets still had plenty of pizzazz last month is the jump in hours worked, an amalgam of total employment and the workweek. Since the workweek jumped sharply from 34.6 hours in December to 34.9 hours—matching October's 7½-year high—total hours rose a sturdy 1%, implying a 4.2% increase at an annual rate from the fourth-quarter average (chart). Even if hours fall back in February, the figures still suggest economic growth of better than 3%.

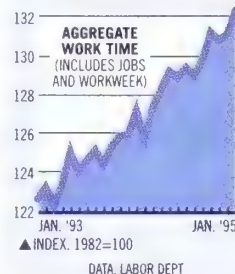
Moreover, average hourly earnings rose 0.6% in January. That's a sizable increase. Together with the surge in hours worked it implies that personal income posted another strong advance last month. Consumers' buying power already has plenty of momentum. Real aftertax earnings had jumped 7.4% at an annual rate in the fourth quarter, far ahead of the 4.6% advance in spending. That's strong support for first-quarter outlays.

Borrowing—just where you would expect to see the results of Fed tightening—is speeding up. Bank loans in the first four weeks of January soared \$32 billion. Commercial and industrial loans, an indicator of inventory investment, accounted for about half the increase, suggesting that businesses are still laying in new stockpiles at a rapid clip. Personal loans have slackened off a bit, but consumer installment debt still rose a hefty \$7.4 billion in December, down from November's mammoth \$12.2 billion increase.

A LOT OF CHURNING in the payroll numbers in recent months has distorted the true trend. Retailers added only 12,000 workers in January, but they had put on 81,000 in December and 132,000 in November—a holiday-influenced result. Also, government employment fell in both December and January after a sharp increase in November, reflecting temporary election workers and the January layoffs of temporary postal employees.

On balance, payroll gains during the past three months have averaged 293,000 per month. That's actually faster than the 241,000 per month in the previous three months. And despite the small January job increase, the percent-

NO SLOWDOWN IN HOURS WORKED



age of industries adding workers actually increased from 59.4% in December to 60.5%, implying that the month's job weakness was narrowly based. All this suggests that February payrolls will rise strongly, or that the January job count will be revised upward.

Manufacturing payrolls are actually gaining steam. Factories added 39,000 jobs in January. The three-month average of payroll increases has been accelerating since last year. Indeed, factory overtime rose to a postwar record of 4.9 hours.

That makes sense. Factory orders ended the year with two strong gains, and the backlog of unfilled orders has risen sharply since August. These trends mean that industrial output in January, to be reported on Feb. 15, scored another solid gain, pushing the capacity utilization rate up from December's 15-year high. As long as operating rates continue to rise, the Fed will remain uneasy about future inflation.

JANUARY'S BIG WAGE increase is sure to catch the Fed's eye. Of course, the monthly earnings numbers bounce around a lot, but looking over the past six months, wage growth has sped up to an annual rate of 3.8%, up from only 1.6% in the previous six months. For half-yearly periods, it's the fastest pace in 4½ years. That's a bad sign, especially since the economy is now entering the stage of an expansion when productivity growth begins to

slow. The result is upward pressure on inflation's most basic fuel—unit labor costs.

Nonfarm productivity, measured as output per hour, rose 1.8% in the fourth quarter, about half the third-quarter pace. Looking at the trend, yearly productivity growth fell to 1.4% in the fourth quarter after peaking at 3% in the first quarter. That dropoff is the consequence of adding 3.5 million new jobs last year.

As a result, the yearly pace of unit labor costs picked up, to 2% last quarter after almost no growth during the year ended in the first quarter (chart). So far, the pace of unit costs remains slightly below the rate of inflation, but any further acceleration will start to push up prices or squeeze profit margins.

So until the Fed gets more concrete evidence that the slowdown is broadening, the risk of more rate hikes this year remains. Remember, the Fed never makes policy based on its, or anyone else's, forecast. When Fed Chairman Alan Greenspan said he would prefer policy to err on the side of restraint, he was saying the Fed will need proof that growth is slowing to a noninflationary pace. The January employment report just doesn't fill that bill.



EUROPE

PRESSURE ON THE BUNDESBANK IS RISING

Germany's industrial sector ended 1994 with an unexpected head of steam. That brightens the economy's prospects in 1995 but raises the chances that a hike in interest rates by the Bundesbank will come sooner rather than later.

New orders taken by west German manufacturers increased a surprisingly large 2.7% in December. For the year, new orders grew 10.8%. Demand continues to rise from both international and domestic markets (chart). For-

foreign orders were up 2.9% in the month, while domestic bookings advanced 2.6%.

Among domestic orders, the biggest gain came from capital

goods, reflecting the drive to lift productivity, while consumer-goods orders fell. Households spent strongly in the third quarter, but now they are feeling the pinch from a January income-tax surcharge and high unemployment. Meanwhile, the January jobless rate rose to a surprisingly high 8.9%, from 8.5% in December.

German manufacturers need demand at home to keep rising because export growth may soften over the course of 1995. The

drag will come mainly from the slower growth in the U.S. and Britain, which together buy 15% of Germany's exports, according to data from the International Mon-

etary Fund. Luckily for Germany, its exports shouldn't be hurt by the spillover of the Mexican crisis. On about 3% of its shipments go to Latin America. Helping to lift exports will be the growing economies in Europe and Asia.

For now, monetary policy remains on hold. At its Council meeting on Feb. 2, the Bundesbank kept interest rates steady, even though the U.S. Federal Reserve and the Bank of England had hiked rates that week. High joblessness and the resultant downward pressure on wage demands, combined with the slowdown in the M3 money supply to 5.7%, putting M3 within the Bundesbank's target, argue for a "steady hand" policy. But the strength in Germany's industrial sector raises the pressure on the Bundesbank to move rates up.



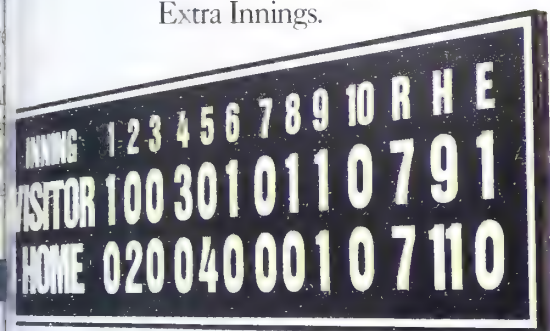
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TRADE

EYEBALL TO EYEBALL WITH CHINA

Clinton is hanging tough—and business is backing him up

Chrysler Corp. is no Johnny-come-lately to China, having spent the past 10 years building a presence in the fast-growing economic superpower's market. With a Jeep assembly plant in Beijing and a shot at a \$1.2 billion deal to build minivans in Guangdong province, the No. 3 U.S. auto maker has a lot to lose if Washington's dispute with Beijing over copyright piracy erupts into a full-blown trade war.

But Chrysler doesn't want American negotiators to go easy on China. The reason: company officials' stunning discovery last year that a Chinese factory a few miles down the road from its Jeep operation was turning out Jeep knockoffs. When Chrysler complained, recalls an outraged President Robert A. Lutz, "the Chinese response was 'Well, we're developing an auto industry, and you should help us.'" To top it off, Chinese officials proposed that, as a condition of winning the minivan contract, the company allow China to market worldwide the Chrysler minivan parts it would produce.

SIGNS OF HOPE. Lutz's fury goes a long way toward explaining why a clutch of industry leaders flanked U.S. Trade Representative Mickey Kantor on Feb. 4, when he announced \$1.1 billion in sanctions against Beijing. Rampant Chinese piracy of American intellectual property isn't just about bootlegged copies of Microsoft Windows and bogus Mickey Mouse logos. While U.S. software companies, moviemakers, book publishers, and the music-recording industry estimate illicit Chinese goods cost them almost \$830 million in lost sales in 1993, the problem is a potential threat to all U.S. industries—everything from prescription drugs to cornflakes. "Everyone operating in China has a baseline fear that once the technology and management knowhow are transferred, the Chinese will try to squeeze you out," says Richard A.

Brecher, an official with the U.S.-China Business Council in Washington.

The penalties Kantor imposed take effect on Feb. 26 unless talks that resume on Feb. 13 produce a settlement—as is now expected. Without a détente, Beijing will retaliate with tariffs on American-made cigarettes, videotapes, compact disks, and alcohol and will for-

mally suspend joint-venture talks with U.S. auto makers.

There are reasons to hope a deal will be cut. Despite the saber-rattling, most normal trade exchanges continue. For instance, Energy Secretary Henry O'Leary plans to lead a group of 50 U.S. executives to China Feb. 19-24 to pursue energy deals. And Chinese TV has be-

TRADE WAR?

Rampant piracy of American products costs U.S. auto makers. The breakdown: Music, \$345 million; software, \$345 million; and other products, \$140 million.



WHAT'S AT STAKE FOR CHINA

Punitive U.S. tariffs could be applied to some \$1.1 billion of Chinese exports to America, including footwear, bicycles, cellular telephones, fishing rods, and plastic picture frames.

ing officials destroying illegal knock-off of U.S. products. There are even reports that some counterfeiters have been executed. Both are signs the government may be cracking down on ripoffs. But even if the current impasse is solved, continued friction between the nations is inevitable. Human rights in China have deteriorated, U.S. initiatives to curb Chinese missile-traffic have hit a wall, and the Chinese balked at a U.S.-led effort to get to adopt global commercial practices as a condition of membership in the World Trade Organization. One key reason is that the imminent death of Deng Xiaoping has paralyzed China's leaders. They don't want to be seen caving in to Washington lest that jeopardize their chances for advancement.

MONEY. What's more, China's mercantile industrial policies dramatically add the potential for friction. To cultivate its own industries, Beijing limits foreign participation in key sectors such as autos, power generation, and telecommunications. And it maintains tariffs and other

barriers that shut out foreign goods ranging from citrus fruits to movies.

Little wonder, then, that U.S. business leaders decided they had to go along with a hard-line policy toward China. In late December, Administration negotiators quietly began asking U.S. trade groups if they would send representatives to Beijing to make their case directly. "We were concerned that the Chinese leadership would miscalculate," based on last year's battle over renewal of China's most-favored-nation (MFN) trade status, says a senior U.S. trade official. Back then, a revolt by business forced President Clinton to abandon his policy of linking China's MFN status to its human-rights record.

At a Jan. 12 meeting with Kantor and three top aides, leaders of a half-dozen intellectual-property associations formally agreed to make the trip. The group, led by Jack A. Valenti, the president of the Motion Picture Association of America, arrived in Beijing on Jan. 20 for two days of meetings with officials of three ministries. In between, they ex-

changed notes with USTR negotiators. "It deprived the Chinese of the opportunity to divide and conquer," says Kenneth Wasch, executive director of the Software Publishers Assn. "We were all singing from the same songbook."

Close coordination with business paid off in other ways. Companies supplied U.S. negotiators with a catalog of piracy horror stories that embarrassed Beijing. From Microsoft Corp., they learned that Shenzhen Reflective Materials Institute, an industrial lab at state-run Shenzhen University, was churning out counterfeit holographs like those the software giant affixes to its program packages. Microsoft says it has lost \$26 million in sales of counterfeit software—but a Chinese court awarded it only \$2,600 in compensation. Record companies identified 29 rogue factories cranking out 75 million counterfeit compact disks annually. And the MPAA passed along taped copies of *The Lion King* and other movies sold in Beijing before their official videotape release.

"GOOD SOLDIERS." When such blatant examples of illicit products failed to get China to budge, the Administration crafted retaliatory sanctions in a way that minimized the damage to U.S. industry and consumers by penalizing Chinese products that are available from other sources. Footwear, which U.S. companies produce in large quantities in China, was targeted, but only children's and women's shoes are affected. Because shoes for men were excluded, the proposed sanctions represent "a very, very small percentage of what we make in China," says a spokesman for Nike Inc.

Given the Administration's considerable leverage, the odds are good that Beijing will move to resolve the dispute. In 1993, Americans snapped up more than a third of China's \$100 billion in exports. Without easy access to the U.S., China's global trade surplus would turn into a net deficit, says Kenneth DeWoskin, a University of Michigan professor.

Many executives remain edgy about the prospect of a trade war. But for now, even those with megadeals at stake are putting their interests aside. "We have to be good soldiers and back [Kantor]," says Lawrence W. Clarkson, a senior vice-president at Boeing Co., which sold one of every seven planes it produced in the past two years to China. Now it's up to the Clintonites, who in the past have talked tough on trade but carried a wet noodle, to show that this time they're prepared to fight.

By Amy Borrus, with Douglas Harbrecht in Washington, James B. Treece in Detroit, and bureau reports

\$330 million in lost sales in 1993. Books, \$110 million; movies, \$50 million.



WHAT'S AT STAKE FOR THE U.S.

If the dispute isn't settled, Beijing could hike tariffs on \$1.1 billion worth of U.S.-manufactured compact disks, video games, Hollywood movies, cigarettes, and alcohol. It also may suspend joint-venture talks with Detroit carmakers.

SANCTION SUBJECTS: REPAIRING A CHINESE-MADE BICYCLE IN NEW YORK CITY; THE MARLBORO MAN COULD GET BURNED IN SHANGHAI

COMMENTARY

By Howard Gleckman

THE BUDGET: CLINTON SHOULDN'T STOP THE SURGERY

Just five years ago, a Democrat who dared send Congress a budget resembling the one President Clinton unveiled on Feb. 6 would have been denounced as a traitor to the party. Clinton's blueprint for fiscal 1996 proposes to kill 130 programs, holds the line on most others, turns over huge chunks of the Great Society to the states, and slashes federal payrolls by 170,000 by next year. On top of that, it would cut taxes by \$56 billion through 2000.

While Republicans quickly denounced the President's fiscal plan as a cosmic punt, in some ways it goes way beyond anything that was offered by his GOP predecessors. By freezing all spending except interest payments and entitlements such as Social Security and Medicare, Clinton would put tighter strictures on the "discretionary" portion of the budget than either Presidents Bush or Reagan. For instance, Reagan proposed increasing discretionary spending by 6.7% in 1982, while Clinton would trim such outlays by about 1% in 1996. Many of the Clinton cuts were sought by Reagan and Bush—and rejected by Congressional Republicans and Democrats as being too deep.

DID HE BLINK? But history doesn't hold much interest for Clinton's Republican critics. Senate Budget Committee Chairman Pete V. Domenici (R-N.M.) gripes that "the President took a walk" on tough cuts. His House counterpart, Representative John R. Kasich (R-Ohio), says that Clinton "came eyeball to eyeball with change. And blinked." Even the Senate Budget Committee's ranking Democrat, Nebraska's J. James Exon, grumbles that the budget "falls way short" of fiscal prudence.



PILE OF CHANCES: The President needs to show he can lead

Clinton's chief problem is that the fiscal debate has moved so far to the right since the November elections that he looks hopelessly behind the curve. And he surely could have done more. While congressional Republicans talk about balancing the budget in seven years, Clinton would allow the deficit to settle in at about \$200 billion a year for the foreseeable future. That's because protected entitlements account for half of all spending and are the fastest-growing portion of the budget. Nearly all of the \$73 billion in added spending next year is due to just three programs—Medicare, Medicaid, and Social Security.

The President ducked tougher cuts because his advisers convinced him that the hard choices should be left to the GOP. He figures public fury over specific spending cuts will overwhelm support for the idea of a balanced

budget. "It makes sense when you look at recent elections," says Price Waterhouse budget analyst Stanley Collender. "Bush tried to cut the deficit and lost. Clinton cut the deficit and the Democrats got no credit in November. Reagan increased the deficit and won."

In the short run, such maneuvering may pay off. The President can watch the Republicans choke on their incompatible vows to cut taxes, protect Social Security and defense, and balance the budget.

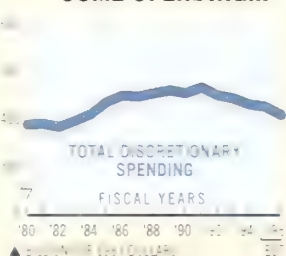
Already, the House GOP has been forced to delay a rollout of its own fiscal plan until April. In part, that's because Republicans fear the bloody details would spook senators now debating the Balanced Budget Amendment. But they also are finding \$1.5 trillion in spending cuts darned hard to come by.

START TALKING. Ultimately, though, Clinton will have to compromise with the GOP. Budget Director Alice M. Rivlin hints that the White House might be willing to deal with Republicans over deeper spending cuts. The budget, she says, is "the start of a dialogue."

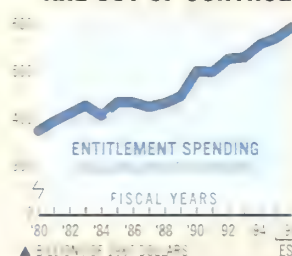
Clinton already has brought the deficit down from \$290 billion, or 4.9% of gross domestic product, to \$203 billion, or 3.1% of GDP. Now, he ought to be able to wring out an additional \$100 billion a year in red ink. He could pull that off by putting together a bipartisan deal on trimming health-care costs. For a President who badly needs to show the public that he can lead, such a strategy might prove smarter than scoring quick political points over the GOP's fiscal agonies.

Senior Correspondent Gleckman keeps track of the budget battles from Washington.

CLINTON IS CUTTING SOME SPENDING...



...BUT ENTITLEMENTS ARE OUT OF CONTROL



DATA: OFFICE OF MANAGEMENT & BUDGET

ILY THE CRAZY IN LOVE THIS TOWN

es and crime rates are high, but the panhandlers are polite

ou've got to love this place. I certainly do. Why else would I be here? You think I'm crazy?

is no cakewalk, living in Washington. e, the District of Columbia has tried to seize my home and auction it off for delinquent taxes and fines. Except they got the wrong house. No apologies, though. Only a snarly rent-a-cop unsnap his Mace holster ominously when I go to City Hall to complain. Like all residents, I'm used to such treatment. Once, my car was towed from a

ctly legal spot in a hip Georgetown neighborhood. ere should have been a 'No Parking' sign there," a police officer explained with irony. I once got a 100 ticket for driving on a snow emergency route—s before the first fell.

DROP. If I didn't live in D.C. so much, I'd be moving out. Nobody else is. In 1980, there were 200,000 residents. Now, just 570,000. What's leaving? The middle class. In 1985, there were 320,000 residents here who were taxed and paid taxes by 1993, just a 22% drop. Such a declining tax base, no wonder

ity is facing a \$722 million deficit and a probable bankruptcy. On Feb. 2, Mayor on and a federal takeover of Medicare, hospitals, and prisons. Why is everyone bolting? It probably has something to do with taxes. D.C. rents pay some of the highest per capita individual, corporate, and property taxes in the nation. Spending is im- mense, too: two times that of Boston, which is approximately the same size, not correcting for state payments. Maybe it's the city's crime rate that has people scurrying for the 'burbs. The District had the highest murder rate in 1992. And what other city sports

a convicted crackhead as mayor? Barry sought reelection by promising prisoners earlier parole and an "Office of Offender Affairs" staffed by released inmates. All presumably on the theory that many D.C. families would vote for Barry just to get their men out of stir and into a job. Evidently it worked, since Barry won a fourth term. But Barry's early-release program wasn't really necessary. One out of four halfway-house inmates simply walk away, city officials admit.

The police do what they can. But

media consultant, was so angry he wrote *D.C. By the Numbers*, a 251-page compilation of shameful statistics that places D.C. at the bottom of nearly every indicator. "Never have so many spent so much and accomplished so little," says Edmonds, who lives on crime-plagued Capitol Hill. William A. Niskanen, a neighbor and chairman of the libertarian Cato Institute, says D.C.'s government is America's second worst, after Detroit. D.C. spends twice the national average per resident "without providing a single high-quality government service," he says.

PLENTY OF SKY. Now a new solution—my personal favorite—appears to be gaining support: Grant D.C. the same status as Guam, American Samoa, and Puerto Rico, America's other Third World holdings, and exempt it from federal income taxes—a \$1.6 billion windfall. House Majority Leader Newt Gin-

THE ADAMS MORGAN AREA IN WASHINGTON



"Twice, D.C. has tried to seize my home and auction it off for delinquent taxes. Except they got the wrong house"

their hearts don't seem to be in it. When Asian-American shopkeepers in my neighborhood complained of a string of armed robberies that left nine of their number dead, Police Chief Fred Thomas suggested they close their shops earlier and "give up a few dollars."

D.C.'s level of corruption can also be breathtaking. A federal probe of the District's public-housing office found that almost everyone who received rent subsidies in 1991 and '92 had to pay kickbacks, often from \$500 to \$1,000. During Barry's first three terms, 11 top city officials were convicted of corruption.

Not everyone flees, of course. Some just complain. Thomas N. Edmonds, a

grich wants to turn the residential portions of the city over to Maryland. Meanwhile, the White House has formed a "working group" to monitor the District's financial travails.

So why live here? Well, the panhandlers are polite. The city's building-height restrictions mean you can always see the sky. People here aren't as beautiful as in L.A. or as well-dressed as in New York, but they're lots smarter. I've met astronauts, spies, Holocaust survivors, mystics, and the real Barney here.

Besides, who'd buy my house?

PAUL MAGNUSSON

Magnusson has lived in Washington for 15 years.

REAL ESTATE

BIG BLUE'S WHITE-ELEPHANT SALE

Putting old properties on the block is saving IBM billions

The I. M. Pei-designed building in Purchase, N. Y., once headquarters for its sprawling U.S. operations, fetched an estimated \$75 million. Its prestigious Madison Avenue office tower went for \$200 million. The posh country club on Long Island's north shore brought in an additional \$10 million.

Acre by acre, IBM is shrinking. Last year, Big Blue sold off 25 properties, quietly dumping 20 million square feet of offices, factories, and research labs—about 13% of the space it owns or leases around the world. That works out to an area twice the size of Manhattan's two 110-story World Trade Center towers. The savings: \$1.75 billion, on top of the \$1.4 billion from facilities-related cuts in 1993. "This has been one of the significant ways to reduce cost and expenses—not just by laying people off," says Bob Djurdjevic, president of computer consultant Annex Research.

NOT-SO-HIGH TECH. And nothing, it turns out, is sacred. On Feb. 3, IBM Chairman Louis V. Gerstner Jr. told employees that the company would abandon its 30-year-old corporate headquarters in Armonk, N. Y. Too old to accommodate expanding the use of such Information Age amenities as videoconferencing, personal computers, and cable television, and too costly to rewire, the concrete-and-glass hilltop headquarters will be sold off. In its place, IBM will spend about \$70 million to build a much smaller, state-of-the-art corporate campus elsewhere on the same 450-acre parcel.

Rethinking real estate has become an IBM axiom. After shedding 183,000 employees—27,000 of them in the past year alone—from a high of 406,000 in 1986, IBM simply doesn't need the rambling space it once did. Consolidating space and subleasing, which reduced electrical and heating bills, accounted for nearly half the \$6.3 billion in cumulative cost cuts in the past two years.

Managers now are evaluated, in part, on their ability to shrink property bills.

That's why IBM's mainframe unit balked a few years ago at paying what it thought was an unreasonable rent at a company-owned facility in Somers, N. Y. With top management's blessing, the organization found cheaper digs a few miles away. The IBM Personal Computer Co. has

IBM-owned plant near Stuttgart, many. Salomon Brothers Inc. and John B. Jones Jr. says that's a real change in strategy. "Rather than [the plants] because there doesn't seem to be enough demand, IBM is doing deals with other companies to fill the facilities," Jones says.

ORANGE RUGS. Now comes the part. IBM has promised Wall Street it will cut nearly \$2 billion more in expenses by mid-1996, and analysts wonder what other properties could go on the block. The Armonk headquarters may be a tough sell. Not the sleek office building—the 1960s-era orange carpeting throughout is justly infamous—it may need considerable spiffing up. Gerstner himself, after all, announced to the world that updating old digs would cost almost



ARMONK, N. Y.

ONE-OF-A-KIND HILLTOP HQ

\$25 MILLION

Distinctive suburban setting for corporate headquarters. Near airport, only 35 miles from Manhattan. Grand architectural detail, with marble lobby and glass atrium designed by I. M. Pei. Sprawling 420,000-square-foot building with abundant offices and charming orange carpet throughout. Set on 450 rolling, wooded acres.

consolidated two manufacturing sites into one in Raleigh, N. C. In all, Big Blue has slashed the number of its manufacturing facilities to 19 from 39 over the past two years.

What's more, other factories have begun taking in non-IBM work or have signed up partners willing to share costs. For instance, a joint venture to build semiconductors with Dutch electronics giant Philips will take over an

much as what IBM intends to spend on new building.

"It's a big dinosaur. Who has money to spend retrofitting that entire facility?," says Rita Cohen, owner of RCR Realty in White Plains, N. Y. "They're going to take a real bath on it." All reasonable offers considered.

By Ira Sager in New York

Besides laying people off, "this has been one of the significant ways to reduce cost and expenses"

TIME WARNER DIVIDES ITSELF, CAN IT CONQUER?

Splitting cable makes sense, but U S West may balk

ave for a stint in the Marines, 66-year-old Alan Gerry has lived in tiny Liberty, N. Y., most of his life. He learned how to fish in the surrounding Catskills. His Saturdays are sometimes spent gossiping at the Liberty diner. Indeed, Gerry would blend right into his hometown except for one thing: He's built a \$2.6 billion cable-TV empire called Cablevision Industries Inc. without issuing so much as a share of public stock. "We're probably a little proud of it," he says.

On Feb. 7, Gerry swapped his equity in Cablevision for shares of Time Warner Inc. Now, his name is subject to Wall Street's ever-changing opinion of Time Warner Chairman Gerald M. Levin. Valued at upwards of \$600 million in a stock deal, the deal has Time Warner assuming \$2 billion in Cablevision debt, Gerry's stake in the company on this gamble: Can a complex strategy hatched by Levin to restructure the company finally make Time Warner's stock take off? "I'm not overly concerned," Gerry says.

Some think he should be. If the Cablevision acquisition and other recent moves go through, Time Warner will face lowering \$19 billion of debt. Levin says he will lighten the load by selling selected assets—including a 20% stake in Turner Broadcasting System Inc. and other cable systems representing 200,000 subscribers. He then plans to spin off Time Warner's cable properties, which serve more than 11 million subscribers, into a new company. The rationale: Since cable deregulation has reduced cash flow in the short term, the heavy assets are needlessly dragging down Time Warner's shares. Segregating them would allow investors to enjoy the growth potential of a "clean" entertainment company, while participating in a solid cable/telephone strategy that is still incubating.

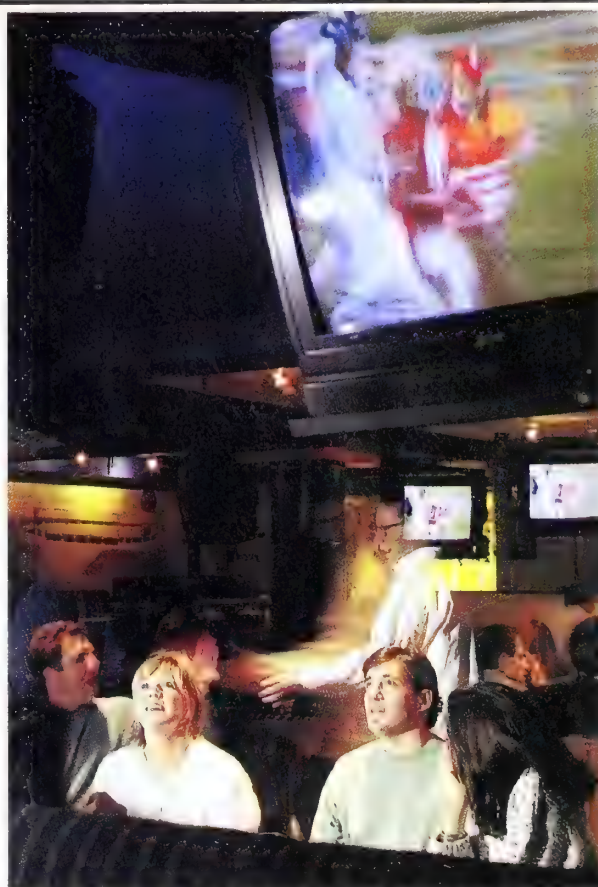
GH NUT. The problem: Most of Time Warner's cable systems already have been placed in a separate entity called Time Warner Entertainment LP. That company, 63% owned by Time Warner, also includes Warner's film studio and its HBO cable channel. The rest is owned by Baby Bell U S West (25.5%) and Japan's Toshiba and Itochu. Figuring true asset values and detaching entertainment properties from the cable assets would be hard enough. Doing so

without diluting or otherwise displeasing shareholders such as Seagram CEO Edgar Bronfman Jr.—who has a 15% share of the common stock—would be harder still.

Under one scenario discussed by analysts, Time Warner could contribute its two most recent cable acquisitions—Cablevision and Houston Industries (both of which it owns outright)—to a publicly traded cable-only company. After much shuffling, the parent company would then keep the entertainment properties for itself. Time Warner Entertainment would disappear.

But why would U S West go for that? Three years ago, the Baby Bell invested \$2.5 billion in the entertainment subsidiary partly to get access to the studio and HBO. Hoping to eventually send video down its phone lines, it wants a source of programming. Analysts agree that U S West's stake in the programming assets alone is now worth more than \$3 billion. "I think it would be very difficult for them to give up" those investments, says a top Time Warner executive.

Many analysts believe Levin likely will have to cede something more to make his partners whole—especially since they're under no obligation to agree to any sort of plan at all. Will he surrender equity in the cable assets? Maybe, but how much is fair to Time Warner shareholders? Does he trade eq-



UNHAPPY HOUR: Cable's cash flow has slowed

uity in the parent? Again, maybe. But that could be dilutive.

The goal likely would be to create two separate stocks that would add up to more value than a single Time Warner share. Says Time Warner finance chief Richard J. Bressler: "Anything we do will create value for all of our constituencies." Still, getting there could conceivably pit the interests of U S West against Bronfman. Bronfman wasn't available for comment, but U S West says it is taking a wait-and-see attitude: "We are very happy with the package of assets we invested in," says Thomas E. Pardun, CEO of U S West Multi-Media Communications Inc. "While we are willing to talk, there is no proposal on the table."

Restructuring or no, Levin's most important tasks are to shave debt and improve cash flow. To help, Levin says he wants to sell \$2 billion to \$3 billion worth of assets within 18 months. But Wall Street may cry for more. "Levin is going to have to get this done," says one former Time Warner executive. "He can't come back in a year and a half and say: 'Sorry, it was too hard to do.'" At that point, even Alan Gerry, like Bronfman, might find himself concerned. Just a little.

By Michael O'Neal in New York, with Kathy Rebello in San Francisco and Ronald Grover in Los Angeles

Cable Spree

Recent cable deals by Time Warner

ACQUISITION	BILLIONS OF DOLLARS	PRICE	THOUSANDS OF SUBSCRIBERS
CABLEVISION	\$2.6		1,300
HOUSTON IND.	\$2.3		1,174
SUMMIT	\$0.3		160
NEWHOUSE	NA*		1,400

*Not Applicable. Joint venture.

DATA: BUSINESS WEEK, COMPANY REPORTS

WORK AND FAMILY

HONEY, WE'RE CHEATING THE KIDS

The child-care crisis is chronic: Can Corporate America cure it?

When Devon Gustafson needed child care for her infant son so she could go back to work, she was disgusted by what she saw. At the home of one family day-care provider, Gustafson, a Metuchen (N.J.) banker servicing mortgages, found a swimming pool with no safety gate. Another left a container of bleach out in the playroom. At a church-run center, Gustafson saw a crying toddler being placed on a pile of rocks—and ignored. "What do you do, except quit and raise them yourself?"

They found that 73.7% of the centers were providing "mediocre" care that may compromise children's ability to enter school ready to learn; another 12.3% were rated unacceptable (table). The findings cut across socioeconomic lines and all levels of the mothers' education.

The lack of quality child care directly affects the productivity of the American workforce. As of March, 1994, according to the Labor Dept., 60% of all mothers with children under the age of 6 were in

Both Republicans and the Clinton administration are mulling plans to force the mothers who head most of the homes to work for their benefits—push them into the workforce by cutting off assistance after two years.

SILENT GOP. Either way, demand for quality child care would dramatically increase—with no corresponding increase in the supply. The federal government spends about \$2 billion a year in child-care grants aimed at welfare recipients and low-income workers. As part of President Clinton's welfare reform plan, he would bolster child-care assistance during job training and the first 12 months off the welfare rolls. The GOP's proposals, while big on fiscal-spending cuts, "don't mention child care," says Bruce Hershfield, director of child day-care services for the Child Welfare League of America. "As a political matter, you can't talk about moving

Day Care's Report Card...

A recent study of 400 day-care centers in four states:

RATING	% OF CENTERS
POOR Children's safety needs not met. No warmth or support from adults observed. No learning encouraged.	12.3%
MEDIOCRE Children's basic needs met. Some warmth and support provided but few learning experiences.	73.7%
DEVELOPMENTALLY APPROPRIATE Health and safety needs fully met. Learning encouraged. Adults have close relationships with each child.	14.0%



...And How To Improve It

The study's recommendations:

- CONSUMER EDUCATION** Teach parents to identify quality child care.
- RAISE STANDARDS** Boost state standards and improve monitoring.
- INCREASE INVESTMENT** Invest in education and training of teaching staff and administrators. Provide pay appropriate to experience and duties.
- ASSURE FINANCING AND SUPPORT** Help families pay for care with government and private-sector subsidies. Tie government funding to meeting quality standards.

DATA: COST, QUALITY, AND CHILD OUTCOMES IN CHILD CARE CENTERS

says Gustafson. "For a lot of us, that's just not feasible."

Unsafe conditions. Uncaring providers. Child care in America today is in crisis. Despite increasing alarms, many working parents—and not just the lowest-wage earners—are leaving their kids in settings that jeopardize their health and safety. Studies show that poor-quality care threatens children's cognitive and emotional development. And the risks are greatest in the critical first three years of life. "Child care in this country is seen as a problem for parents and not as an investment," says Barbara Reisman, executive director of the Child Care Action Campaign.

A new study provides vivid details of just how bad care can be—and of the market forces at work. The study, released Feb. 6, of 400 day-care centers was done by economists and child-development experts at four universities.

the labor force. When child care falls through, absenteeism and turnover soar. Says Joan Lombardi, a senior adviser at the Health & Human Services Dept.: "Continuity of child care is a requirement for continuity and productivity of work."

It's also critical for welfare mothers trying to lift themselves up into the workforce. In 1992, the last year for which data is available, 61% of families on welfare included kids under age 6.

**Unsafe conditions.
Unhealthy
surroundings.
Uncaring providers.**

from welfare to work without talking about child care. Someone's going to have to care for those children."

Why is good child care so tough to find? The answer, concludes the recent study, *Cost, Quality, and Child Outcomes in Child Care Centers*, boils down to economics. In the states studied—Connecticut, North Carolina, California, and Colorado—researchers found that even mediocre care is expensive. On average, it costs a center \$4,940 a year—excluding donations—to provide services for one child. That represents 8% of the 1993 median U.S. family per capita income for a dual-earner family, and 23% of earnings for families headed by a single parent working full-time.

Trouble is, child care is an imperfect market: The study found that strong competition in local markets keeps a tight lid on prices—but it also depresses the quality of care provided to children.



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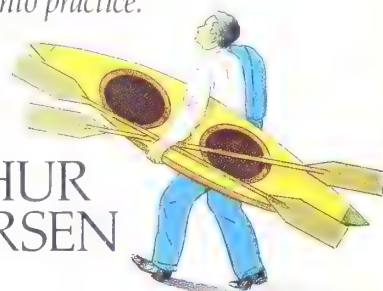
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dren. Centers have little incentive to boost quality because providing good care costs about 10% more, the study found. Higher-quality centers, for example, typically have lower ratios between adults and children, and employ better-educated teachers who earn more.

What's more, parents overestimate the quality of care kids receive. The study found 90% of parents rated programs as "very good," while trained observers rated most of them "poor to mediocre." But it also found that parents aren't really demanding quality, perhaps because of the "inherent difficulty" of monitoring care. What parents asked for—and got—were longer hours, from after-school programs to summer camps, to allow for job flexibility.

COMMITMENT CARROT. Increasingly, companies are responding to the gaping need for good child care—a move the study applauds. Researchers found that the 16 workplace centers they observed adhered to higher standards than many other centers in the study. The key difference: access to extra resources that they used to boost quality.

NationsBank Corp. in 1994 set aside \$10 million for a five-year investment in such programs as its own child-care center and training for employees' caregivers. Workers at Genentech Inc. can use a company-built day-care center, open 12 hours a day. Genentech underwrites half the operating costs. The facility has slashed turnover and lured back employees such as Pamela M. Peters, a mother of three who left in the 1980s, partly because of the trouble she faced finding good child care. "When I wanted to come back to work the No. 1 thing was, did the company have a commitment to working parents?" says Peters.

But Corporate America can't solve the child-care problem alone. So some companies such as Johnson & Johnson are turning to the community. As part of the American Business Collaboration for Quality Dependent Care, J&J and 10 other corporations have enlisted the help of some 145 entities and raised \$27 million to fund dependent-care projects in 45 communities.

Even such collaborative efforts, though, will fall short without a national commitment to ensuring good-quality care for all children. The study calls fostering such a commitment its "one critical recommendation." Given the belt-tightening in Washington when it comes to social programs, working parents like Gustafson shouldn't hold their breath.

By Michele Galen in New York, with Mike McNamee in Washington and business reports

NIMBLE: THE SHUTTLE MAKES 342 TRIPS DAILY



AIRLINES

NOT BAD, FOR A DUMB IDEA

United's Shuttle has put Southwest on notice

Los Angeles architect Richard L. Dachman used to fly Southwest Airlines on his monthly business trips to Northern California. He loved the cheap fares and frequent flights, but hated the lack of elbow room and the "cattle-call" rush to grab unassigned seats. Now, Dachman flies the Shuttle by United instead. His round-trip ticket to Sacramento costs \$84—the same as Southwest's fare—plus, he enjoys an assigned seat and can use frequent-flyer miles to upgrade to first class. "This is a lot more organized," Dachman says.

A deranged MBA's pipe dream, a suicide mission—at the very least, a dumb idea. That's what industry consultants and airline executives called United Airlines Inc.'s plan to launch a short-haul carrier in California, the heart of Southwest Airline Co.'s short-haul system. If nothing else, says Michael J. Boyd, president of consultant Aviation Systems Research, "the Shuttle is a distraction that keeps them from focusing on their core problems. Starting a second airline doesn't fix the first one."

The thing is, United's California dream is making headway. Armed with wage cuts from an employee buyout in July, United launched the Shuttle in October. Four months later, the service is stealing Southwest's passengers and reducing profitability on some of its most traveled routes. Citing fare wars and

lower profit per passenger, Southwest reported fourth-quarter profits down nearly 47% from a year earlier, to \$2 million.

The Shuttle is still hitting some bumpy patches. On-time performance has slipped badly since October because of persistent bad weather. And with more flights operating, passenger load factors have dropped, from 70% in October to 60% in December. Southwest has declined, too, but not as much.

Indeed, analysts think United is losing millions on the Shuttle, though the company won't break out data. The line may not turn a profit on its own unit until 1996. Says Southwest CFO Financial Officer Gary C. Kelly: "United and the rest of the industry have made significant progress in reducing costs, but I don't see them matching us."

WHY DRIVE? In the meantime, travelers are reaping the benefits. Air fares on the hotly contested Los Angeles-Oakland corridor have plunged to as low as \$35 one-way. "At that price, it's cheaper than gasoline," says Lawrence R. Crawford, president of Avitas Inc., Reston (Va.) airline consultant. From December, 1993, to last December, the San Francisco-Seattle route, coach one-way fares dropped 74%, to \$139, according to the American Express Airfare Index.

Both airlines are stepping up flights, too. The Shuttle makes 342 trips daily among 15 cities—all but three of them in California—up from 184 flights in October. Southwest, still king of the West, offers 465 flights in and around the Golden State—up from 433. Who will blink first? Neither rival will give in easily, analysts say. That means California's blue skies could be filled with red ink for months to come.

By Susan Chandler in Chicago, with Eric Schine in Los Angeles



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GENERAL MAGIC'S SPELL

An Apple spin-off's IPO makes a stir despite perils ahead

It feels a lot like biotech. Lots of promise. No track record. Nonetheless, any day now, General Magic Inc., a Silicon Valley software maker with zero profits, a whisper of revenues, and very big dreams, plans an initial public offering that has Wall Street buzzing. The early line: This IPO could rise well above its expected \$13-a-share offering price.

Why? The 1990 Apple Computer Inc. spin-off is one wellborn toddler. Two of its three founders, Andrew Hertzfeld and William Atkinson, helped create the Macintosh. The third, Marc Porat, is a Silicon Valley visionary who championed anytime, anywhere communications at Apple. General Magic's investors—who already have ponied up \$77 million—read like a high-tech Who's Who: AT&T, Sony, Motorola, Matsushita, and Toshiba, to name a few. And the company operates in a white-hot field: software for

wireless communications. Says Motorola Vice-President Randy Battat: "This is a long-term, huge opportunity."

But it may be a long time before the opportunity pays off. A \$13 stock would give General Magic a market value of some \$300 million. Yet it has revenues of just \$2.5 million—from two products largely unproven in the market. Its Magic Cap software for "personal communicators" lets people send and receive E-mail and faxes by tapping on the screen of a handheld device. Then, there's Telescript: a programming language for communications software that enables software "agents" to zip along I-ways to retrieve data.

TOO EARLY? General Magic hopes to be the standards-setter in personal communicators—a sort of Microsoft Corp. of the handheld market. Trouble is, Microsoft plans to be that, too, as do Apple and software maker Geoworks. Meanwhile, the market for personal communicators has yet to jell. Says Nathan P. Myhrvold, senior vice-president of Microsoft's Advanced Technology Group: "General Magic is going to miss

the window. Their effort is way too early. I can't imagine how they will be successful."

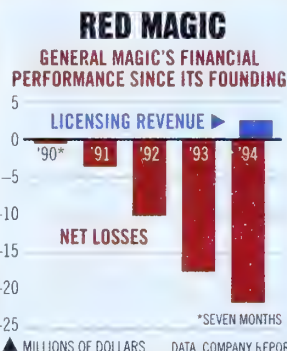
General Magic's answer is to develop versions of Magic Cap that run on personal computers. That way, handheld devices using Magic Cap will be able to swap info with PCs. The new Magic

Cap versions are set to debut this summer. To leverage its marketing muscle, the company is counting on its big partners to license its software for their own products. So far, though, only a handful have stepped up to the plate.

Meanwhile, analysts figure General Magic is spending \$2.5 million a month. Red ink date: \$53.1 million. A

its prospectus says it expects "substantial" losses through '96. The 4 million share IPO will sell less than 20% of the company, raising some \$50 million. Insiders expect that, plus \$34 million in cash on hand, to carry General Magic into '97. Could be. But investors may have jittery moments before its fundamentals match the hype around it.

By Kathy Rebello in San Francisco

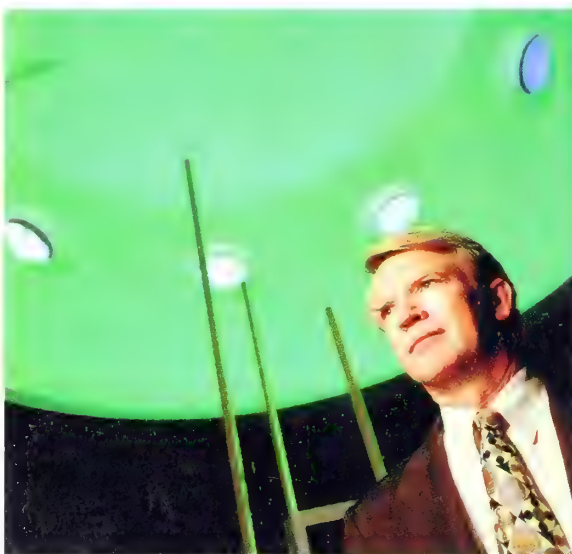


DEALS

RUMBLE IN TOONTOWN

Silicon Graphics drops a bundle to one-up Microsoft

A showdown is shaping up in Hollywood that would do Gary Cooper proud. On Feb. 7, Silicon Graphics Inc., whose graphics computers helped create the special effects in *Jurassic Park*, *Forrest Gump*, and other movies, said it will shell out \$500 million in stock for two computer-animation software companies, Wavefront Technologies Inc. and Alias Research Inc. And Hollywood sources say SGI already is trying to talk filmmakers into adopting the new technology it is assembling. Among the companies that have been approached, says SGI CEO Edward R. McCracken, is DreamWorks SKG, the new studio that teams Jeffrey Katzenberg, Steven Spielberg, and David Geffen. Neither side will confirm that a deal is imminent.



SGI'S McCRACKEN: Foresees all-digital film studios

Why SGI's big move on Tinseltown? In a word, Microsoft Corp. Last year, the software giant bought Softimage Inc., a rival to Alias and Wavefront. The prize both companies covet: control of the tools to build interactive TV, video games, and online information systems. Entertainment, McCracken says,

is already "the fastest growing computer market by far."

SGI, with its powerful computer servers and 3D graphics workstations, hopes to lead a shift to digital movie studios. Alias and Wavefront, which create animation and manage special-effects software, dominate their fields and could give McCracken a clue to standardize digital formats that are a long-standing block to movie digitization.

Microsoft, however, has similar designs. Already, it has announced Softimage deals with Sega Enterprises Ltd., Fox Animation Studios Inc., and others.

And last month, it put pressure on SGI's new partners by dropping prices on Softimage programs as much as 65%. But with SGI's backing, the two companies should be far more formidable foes. Could be a digital *High Noon* in the making.

By Robert D. Hof in San Francisco



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ROBERT HAFT CIRCLES PHAR-MOR

HE LOST THE COMPANY TO Dad, then got mired in an eccentric intrafamily legal fracas. What to do now? Robert Haft, ousted from Dart Group last year by father Herbert, is considering a bid for bankrupt Phar-Mor, sources familiar with his plans say. Haft, who won't comment, is said to be leading a group that hopes to buy a majority stake in the \$1.9 billion discount drug chain, which is seeking to emerge from Chapter 11 protection. The move would give the 41-year-old executive a place to plunk his cash cache in the wake of his departure

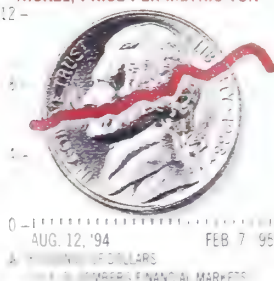
CLOSING BELL

HOT METAL

Blame it on the Siberian winter. The price of nickel, a metal used in stainless steel and the U.S. coin, has soared 80% since August, in part because of weather-related production shortfalls at the huge Norilsk refinery on the remote Russian tundra. Add in surging demand and a scrap shortage, and you have a mecca for speculators. On Feb. 6, a correction blew off some froth, sending prices down 11%. But after more retrenchment, analyst Vahid Fathi of Kemper Securities expects a buying opportunity. By next year, he predicts, prices will be 25% to 30% higher.

NICKEL, PRICE PER METRIC TON

12 -



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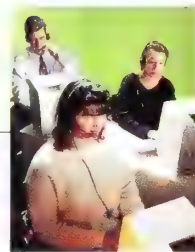
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GEPHARDT IS NOT RUNNING. WELL, NOT EXACTLY

is a testament to the way things have been turned upside down on Capitol Hill that the leader who's keeping the White House off balance the most is not House Speaker Newt Gingrich or Senate Majority Leader Bob Dole. It's House Democratic leader, Richard A. Gephardt, who's making a career out of upstaging President Clinton in a bid for the affections of America's working class. Although he praises Clinton for doing "a good job," Gephardt has rarely missed a chance to pounce while the President pondered. He preempted the White House with his proposal of a middle-class tax cut, seized upon the flat-tax concept, and even delivered his own State of the Union address that replaced Clinton's Middle Class Bill of Rights with a worker-sensitive "Code of Conduct" for U.S. corporations. No wonder Clintonites are sweating. When their man moving to the right, they see Gephardt grabbing the Democratic Party's working-class core, a springboard for a Presidential run.

MOUThPIECE. Gephardt insists he's not trying to undermine Clinton. But despite his leadership post, he won't be a mouthpiece. "It's not my job to say 'absolutely' to yes and every thing the President comes out with," he says. Party insiders believe Gephardt, a failed 1988 White House aspirant, when he flatly denies that he will challenge Clinton for the party's nomination. So what's he up to? Gephardt has three goals. He wants to push Clinton toward a populist agenda that portrays Democrats as defenders of the middle class and Republicans as pawns of the rich. He's creating an independent platform for Democrats who fear they'll be dragged down with a Clinton collapse in '96. And he wants to keep a White House run in his sights—next year, if Clinton bows out, or later. "You're seeing a very shrewd, experienced Presidential candidate position himself in case there's an opportunity," says Democratic consultant Brian



A PAL? He lauds Clinton, but...

Lunde. "On a crass political level, he wants to be first in line."

But with Clinton fighting to keep his job, Gephardt's priority for now is to push the President toward more liberal economic policies. He helped shape Clinton's proposal to raise the minimum wage from \$4.25 to \$5.15 an hour. When White House rhetoric strays to New Democrat dogma about reinventing government and communal responsibility, Gephardt grows impatient: "I'm not one who believes you need to make dramatic downsizing in government."

Instead, he wants to focus on a brand of economics often dismissed by Republicans as recycled "class warfare." Gephardt countered a GOP flat-tax plan with a "flatter tax" that has a 10% rate for the middle class and higher brackets for Corporate America. And in a recent speech to the liberal Economic Policy Institute, he exhorted companies to share more power and profits with productive workers. "You don't have to graduate from Harvard business school to figure this out," he says. His models of company-worker cooperation include Saturn, Anheuser-Busch, Ben & Jerry's, Motorola, Starbucks, Magma Copper, Harman International, and Inland Steel.

Gephardt's high-profile freelancing may irk Clinton less than Al Gore, a bitter 1988 Presidential campaign rival who's trying to stake out the party's right flank. But party liberals think Clinton can only gain. "Gephardt's a very effective populist spokesman," says Democratic consultant Vic Fingerhut. "As more people see Democrats representing their interests, Clinton's numbers will go up, too."

Gephardt is on a political tightrope. The danger of his "I'm-on-your-side" shtick—as the GOP notes—is that it will echo class-warfare appeals that flopped in the Reagan era. But he keeps plugging. Better to start a Presidential bid with a small but solid base than none at all. Just ask Bill Clinton.

By Richard S. Dunham

CAPITAL WRAPUP

RUDE FEUD

Republican Senators Alfonse M. D'Amato of New York and Frank H. Murkowski of Alaska are quietly duking it out over an export ban on Alaskan oil. D'Amato, who favors the ban, won the first battle when the Senate referred the issue to his Banking Committee, while Murkowski, who wants to lift the ban, tried to keep it in his Energy Committee. Why? D'Amato's interest? Northville Industries Corp. in Melville, N. Y., operates a pipeline that carries excess Alaskan

oil to the Gulf of Mexico for sale in the U.S. Northville's political-action committee and its CEO, Jay Bernstein, are past D'Amato contributors.

REINVENTING THE PATENT OFFICE

► The Administration will soon unveil a plan to turn the U.S. Patent & Trademark Office into a government corporation similar to the Postal Service. Clintonites say the proposal, which requires congressional approval, would cut 5,000 federal jobs, save millions of dollars, and streamline patent operations.

CHAIRMAN KANTOR—AGAIN?

► White House political advisers are considering U.S. Trade Representative Mickey Kantor to run President Clinton's reelection campaign. Commerce Secretary Ronald H. Brown was Clinton's top choice, but GOP probes of his tangled finances could make him unsuitable for the visible campaign post. Kantor is likely to take the job if offered. He chaired Clinton's 1992 campaign, and was hurt that the White House first considered Brown instead of him for the '96 post.

Everything you know about
recycling.



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Belzer, 6, son of Jim Belzer,
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Finally, if you've read this far, it's obvious that you'd like to see more progress in recycling. To talk more, call Steve Van Voorhis, Manager of Recycling Programs, at 1-800-831-8354.

INTERNATIONAL  PAPER

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MEXICO

PAUL REICHMANN: IS ANOTHER DREAM DYING?

His ambitious Mexican projects with George Soros have been pounded by the peso crisis

The project was classic Reichmann: highly ambitious, highly aggressive, and high-risk. Elaborate scale models laid out the design: \$1.35 billion worth of real estate developments in and around Mexico City. The plans, which included one of the world's grandest urban developments, were the product of a partnership between beleaguered Canadian developer Paul Reichmann and investor George Soros.

To Soros, the models represented a chance to make a lot of money. But to the 64-year-old Reichmann, they meant far more. The three projects were a bold bid to regain his family's status as one of the world's greatest developers. Their real estate empire, Olympia & York Developments Ltd., once spanned the U.S., Canada, and Britain. But much of that empire was forced into bankruptcy in 1992 after its Canary Wharf office complex in London ran into financial problems.

Just two months ago, Reichmann International, headed by Paul, was expecting its real estate ventures to benefit from the rapid growth that the North American Free Trade Agreement would generate in Mexico. But that expectation has been dashed by the sudden devaluation of the peso that savaged Mexico's economy. Progress on Reichmann's three Mexican projects has ground to a halt (table).

The devalued peso hits Reichmann on a number of fronts. Interbank interest rates have shot up to 45%, making the local financing that the projects counted on far too expensive. Mexican

banks are loath to lend when their own balance sheets are shaky. Meanwhile, foreign capital has stopped flooding the country. And the sudden recession hurts demand for all types of real estate.

Even when demand picks up, Reichmann and others will have to charge more modestly for space. Prime office space in Mexico City went for \$55 to \$65 a square foot in 1994—the highest prices in the hemisphere. Henry McDonald, a director in Cushman & Wakefield

ma Canal Zone. And he has started an Asian division to scout for opportunities. "Nothing has actually jelled yet" when that, says Soslone. "It's a very different market.... Mexico has a much greater tradition of property rights than Canada and a culture we're closer to and can work with more comfortably."

But the squeeze in Mexico will cause some financial pain. The projects are an equal partnership between Reichmann International and Soros. The partners

The Reichmanns' Setbacks In Mexico

ALAMEDA

The \$500 million redevelopment of downtown Mexico City is stalled until cash-short government agencies can sign leases

SANTA FE

The \$500 million, 30-building office, hotel, and condo complex will be built in increments once new equity investors and lessees are found

CHAPULTEPEC TOWER

The \$350 million luxury office building is on hold until a major tenant and international financing are lined up

DATA BUSINESS WEEK

GRAND PLANS

An architectural rendering of the Santa Fe site—once a garbage dump—on the western outskirts of Mexico City



Inc.'s Mexico City office, expects prices to fall around 20% in 1995. Ronald Soslone, director of development for Reichmann International, says the developer plans to forge ahead, but sources say all three projects will be postponed.

LAUNCHING PAD. Even if the projects inch forward, Reichmann's dream of using Mexico as a launching pad to rebuild an empire has been dealt a brutal blow. Reichmann had won a role in a consortium that will draft possible urban-development schemes for the Pana-

have bought six acres of prime downtown real estate for the Alameda project, 20 acres in the Santa Fe district, two acres of top-dollar land in Mexico City for an office tower, and two floors in a posh district for the company's offices.

Apart from saying the amount, "substantial," Soslone will not say how much the Reichmanns have invested. Soros spokesman declined to comment. Since the venture is a private partnership, there is no public information on how much money has been invested.

hmann or Soros. estate analysts say investment in land office space could be \$50 million. bulldozers were prepping terrain at the site of a Fe project in Mexico City, when the Mexican peso was devalued. The complex is to serve as a city center for a corporate and commercial development on the outskirts of Mexico City. But local financing problems are slowing the development. Instead of being built on speculation, it now has to be built in stages, as demand financing allows. Reichmann and joint-venture partner Mexico's largest construction company, are also seeking committed ten-



PAUL REICHMANN
Managing Director

ants and another equity partner before building the office towers. But efforts to have a Mexican bank join in as a financing and equity partner have been complicated by the devaluation. "The few resources banks have must be used to restructure loans or finance liabilities," says Pedro A. Azcue, general director of La Salle Partners, real estate agents in Mexico City.

STATE CUTBACKS. Reichmann's 52-story luxury office building also faces big hurdles. With local financing all but nonexistent, Reichmann must sign up blue-chip tenants, preferably foreign companies, before even seeking international financing. Work was supposed to start in February but has been indefinitely delayed.

The future of the Alameda urban-redevelopment plan is perhaps the most uncertain. It will only proceed if government agencies commit to taking big chunks of space. But spending cuts may prevent that.

The projects are unlikely to go into total meltdown. Real estate analysts expect demand for top-class office space to pick up once the Mexican economy starts to recover. "We think there is going to be a market for office space in three years, when the buildings will be finished," says Soskolne. "We're working very hard to make it work."

Hard work alone won't do the job. Neither Reichmann nor Soros can control world currencies or economies. And those factors will decide the fate of Paul Reichmann's comeback bid.

By Geri Smith in Mexico City, with Suzanne Woolley in New York

COMMENTARY

By Dean Foust

WHAT THE IMF NEEDS IS A GOOD ALARM SYSTEM

The morning after the International Monetary Fund had stepped into the breach to help Mexico avert a government default, IMF Managing Director Michel Camdessus was already congratulating himself. "The IMF has risen to this challenge with assistance in an exceptional scale," he said of the fund's \$17.8 billion loan to Mexico—by far the largest it has ever made.

Despite Camdessus' boast, the Mexican affair was not the fund's shining hour. True, the IMF loan—part of a \$49.8 billion bailout engineered by the group of Seven industrial nations—staved off a global financial panic. But where was the IMF six months ago, before Mexico's deteriorating situation turned into a crisis? Casting out a global safety net

is well and good, but Camdessus' top priority should have been operating an early warning system that detects problems in emerging economies before they become catastrophes.

LOWING FREELY. Camdessus seems intent on making the IMF a central bank for the world, but the Mexican panic suggests a more critical role: The IMF should become a global Securities & Exchange Commission that exerts pressure on governments

to provide full disclosure of their financial health. With capital flowing freely into exotic markets from Bangkok to Buenos Aires, investors need greater assurances that emerging nations aren't harboring nasty financial secrets.

The IMF conducts rigorous surveillance of 60 countries with outstand-

ing internal analysis is stamped "confidential," and not one of these documents has been declassified in the 49-year history of the institution.

REFRESHING CANDOR. IMF officials contend that sounding the alarm too loudly can itself trigger a panic. True, but it's still better to deal with a brewing problem sooner than later.

"If the IMF had been more candid about Mexico's problems, it would have caused this crisis a year ago—but the situation would have been much smaller and more easily contained," says David Hale, chief economist for Kemper Financial Services Inc.

To its credit, the IMF seems ready to mend its ways. On Feb. 7, Camdessus vowed to increase surveillance of economies in "convalescence" to avert

future panics—and he confessed that 10 unidentified ones could be headed for crises this year. For the fund, the quintessential immovable bureaucracy, even such a limited display of candor is refreshing. Now it's time for the IMF to adopt a new role as global capital cop—and Camdessus soon should start naming some suspects.

Foust covers international economics from Washington.



MADNESS AT THE MERC: Can currency panics be prevented?

ing credit, but the other 119 member nations are subject to lax monitoring. That was the case with Mexico, which gave the IMF outdated reports that masked its dwindling hard-currency reserves.

Beyond improving its monitoring, the IMF must be willing to blow the whistle on irresponsible governments. This means lifting the veil of secrecy that shrouds IMF operations: Nearly every loan document and accompany-

**DEUTSCHE BANK: BOTH
A MAJOR OWNER AND
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GERMANY

SUDDENLY, GERMANS LOVE TO HATE THEIR BANKS

Anger over bank control of industry may reshape the economy

When Deutsche Bank CEO Hilmar Kopper dismissed \$33 million of unpaid bills owed to construction craft workers as "peanuts" last April, he unleashed a new wave of antibank populism in Germany. The workers are victims of the spectacular—and allegedly fraudulent—bankruptcy of the giant Schneider real estate group. The \$33 million is indeed small change alongside the \$3.2 billion that "construction lion" Jürgen Schneider owes to Deutsche and other banks. But Kopper's seemingly callous tone ignited popular resentment against German banks' power.

The flare-up is now turning into a political firestorm. On Jan. 30, the opposition Social Democratic Party (SPD) introduced federal legislation to cut down the banks' sizable shareholdings in key industrial companies to no more than 5% equity stakes. And it would end the banks' power to vote huge blocks of proxies for corporate shares they hold as custodians. Such a move would radically reshape Germany's economy by ending the banks' tight control over wide swaths of the nation's industry.

Adding to the furor, district attorneys are investigating banks on suspicion of money laundering and aiding tax-evasion schemes using foreign havens. On Feb. 2,

federal tax agents raided offices of Bayerische Hypotheken- und Wechsel-Bank searching for such evidence, following an earlier raid on Dresdner Bank. No indictments have been issued, and the banks deny any wrongdoing.

Another powerful impetus for change is coming from outside Germany. The nation urgently needs to tap global investors for huge new infusions of capital. Right now, German capital markets are too puny to finance the coming series of megabuck privatizations of phone monopoly Deutsche Telekom and other state-owned companies.

To attract outsiders to buy into such privatizations means adopting foreign, particularly U.S. and British, approaches to transparent accounting and corporate governance. That will be a major break from the current pattern of clubby ties, shielded from public scrutiny, between corporate Germany and its financial institutions.

Already, the banks' political support seems

to be slipping. Chancellor Helmut Kohl's coalition partner, the Free Democratic Party (FDP), is as eager to see bank power crimped as is the SPD. And now, members of Kohl's own party are leaning toward legislation to rein in the banks.

The banks are vulnerable because of their conflicts of interest. Besides serving as proxies, a bank is often, quite legally, both a major creditor and a shareholder of the same company, with bank officials serving as members of the company's board and even as chairman. Take Daimler-Benz, Germany's biggest industrial group. Deutsche Bank, the country's No. 1 bank, owns 24% of Daimler's shares and is a major lender, while CEO Kopper chairs Daimler's supervisory board.

Trouble is, even though banks may not want to be evenhanded in their multiple roles, German law won't let them. When bankruptcy looms, the law gives priority to creditors, mainly banks, over all other parties. "Under German corporate law, the principle is to protect creditors and not shareholders," says Gerhard Koning, head of corporate finance at Frankfurt's Commerzbank.

BAILOUT LEGACIES. The problem is amplified by Germany's debt-heavy system of corporate finance. Debt-to-equity ratios average as high as 4 to 1, compared with around 1.3 to 1 in the U.S. During the most recent recession, loss of capital quickly pushed many companies to the wall. Cologne-based diesel engine maker Klöckner-Humboldt-Deutz, for example, said on Jan. 30 that it needed a \$605 million bailout. Deutsche Bank holds a 36% stake in KHD, and Kopper chaired its supervisory board until the start of this year.

Such troubles are no surprise to bank critics such as University of Mannheim professor Manfred Perlitz, who says bank-controlled companies perform no worse than those not under bank influence. In rebuttal, the banks argue that many of their equity stakes are

the involuntary legacy of earlier basket-case bailouts. And banks say they don't interfere in day-to-day management.

All the same, pressure for change is increasing. As the global competition for scarce capital heats up, German banks may need to yield some of the power they insist they don't want anyway.

*By John Templeton
in Frankfurt*

WHAT THE BANKS ARE UP AGAINST

New draft law would limit banks' equity stakes in industrial companies to 5%

Spate of corporate bankruptcies and bailouts hurts banks' reputations as company lenders, shareholders, and directors

Pending privatizations are stepping up pressure from abroad for new rules to curb banks' potential conflicts of interest



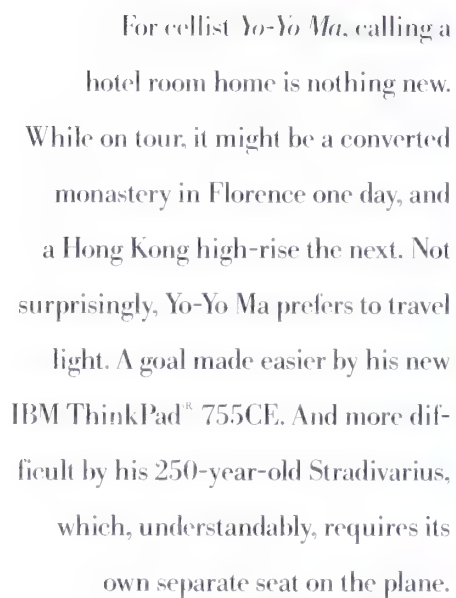
*Statue of President & Mrs. Lincoln,
East Park, Racine, WI.*

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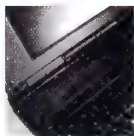
For cellist *Yo-Yo Ma*, calling a hotel room home is nothing new. While on tour, it might be a converted monastery in Florence one day, and a Hong Kong high-rise the next. Not surprisingly, Yo-Yo Ma prefers to travel light. A goal made easier by his new IBM ThinkPad[®] 755CE. And more difficult by his 250-year-old Stradivarius, which, understandably, requires its own separate seat on the plane.



(Yo - Yo)

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LOOK WHO'S MAKING A REVOLUTION: SHAREHOLDERS

Impatient investors go after old-guard Russian managers

Derzhava Fund, a Moscow-based investment firm, was fed up with the managers of Yaroslav Rubber Co., a maker of tires and other car and aircraft parts. Derzhava didn't think they were doing enough to replace military customers. So Andrei Volgin, the fund's head, joined with other outside investors last fall to force a change. They installed a new CEO and a team of young financial experts. In three months, the company has signed new orders equal to last year's sales. "Things can change fast if you can change the management," says Volgin, who is also chairman of the Moscow Committee for Shareholders' Rights.

With capitalism still on shaky terrain, Russia is an unlikely battleground for shareholder rights. Yet over the next three months, old-guard managements at newly privatized companies are going to find themselves increasingly on the defensive. Some 24,000 annual shareholders' meetings are scheduled. Many are likely to turn into showdowns between former state managers and Young Turk private investors demanding better performance. Says Dmitri Vasilyev, deputy chairman of Russia's new Securities Commission: "Many will lose their posts and be replaced by more qualified people." By one estimate, up to 4,800 chief executives could get the boot along with many directors.

YANKED AWAY. The old guard is not going to go quietly. They've lobbied their allies in Boris Yeltsin's government to stall economic reforms. While the Chechen conflict raged, the hard-liners proposed renationalizing some industries and placing curbs on foreign investors.

But there has been a determined counterattack by proreform forces led by Premier Viktor S. Chernomyrdin. The government seems determined to push for reform at the company level, so shareholders will be allowed to install new managements, and subsidies will eventually be yanked away from failing companies.

One can't blame the old-line managers for being upset at the changes. In the Soviet era, all they had to do was please the party bigwigs and meet government targets to get all the trappings of pow-

er, including a limo. Now, some twenty-something investment manager in a spiffy suit could toss them out. "They didn't realize privatization would mean reorganization," says David Reuben, president of Trans-World Metals Ltd., a London-based trading company that has made big and controversial plays in Russia's aluminum business.

But the corporate apparatchiks are quickly learning new tricks to frustrate their opponents. They range from di-



luting the ownership stake of investors to such simple ploys as erasing the names of outside investors from computerized shareholder lists. Or they wrap themselves in the flag, charging that outside investors are speculators or opportunists who want to strip Russia of its wealth.

One investment group that got a nasty surprise was Moscow's Rossisky Credit Bank. When it snapped up a 22% share of Lebedinsky Mining Co. last year, it thought it had a great deal. The mine has modern facilities that produce an iron-ore additive much in demand. But the general director, Anatoli Kalashnikov, denied the bank a board seat and then diluted its holdings by giving big new stakes to a local fish farm and other allies. "He just doesn't want to

lose or share power," says Alexandr Lyubinin, a Rossisky vice-president. Kalashnikov replies that the investors "don't want to participate in real work here, they just want to make money."

Another company whose shift to capitalism has been tied up in knots is Zil, a dinosaur that has been turning out the same basic truck for 30 years. Zil's case the problem is money. Its initial stock distributions raised a measly \$750,000, though Zil occupies 50 prime Moscow acres. Yet to compete on world markets, Zil needs a modernization program costing \$200 million, says Chairman Alexander P. Vladislavlev.

HICCUPS. Shareholders can't agree how to find that kind of money. Vladislavlev, installed as chairman last May, has put together a rescue plan in which a new financial holding company would offer a \$250 million stock issue to fu-

JURASSIC TRUCKS

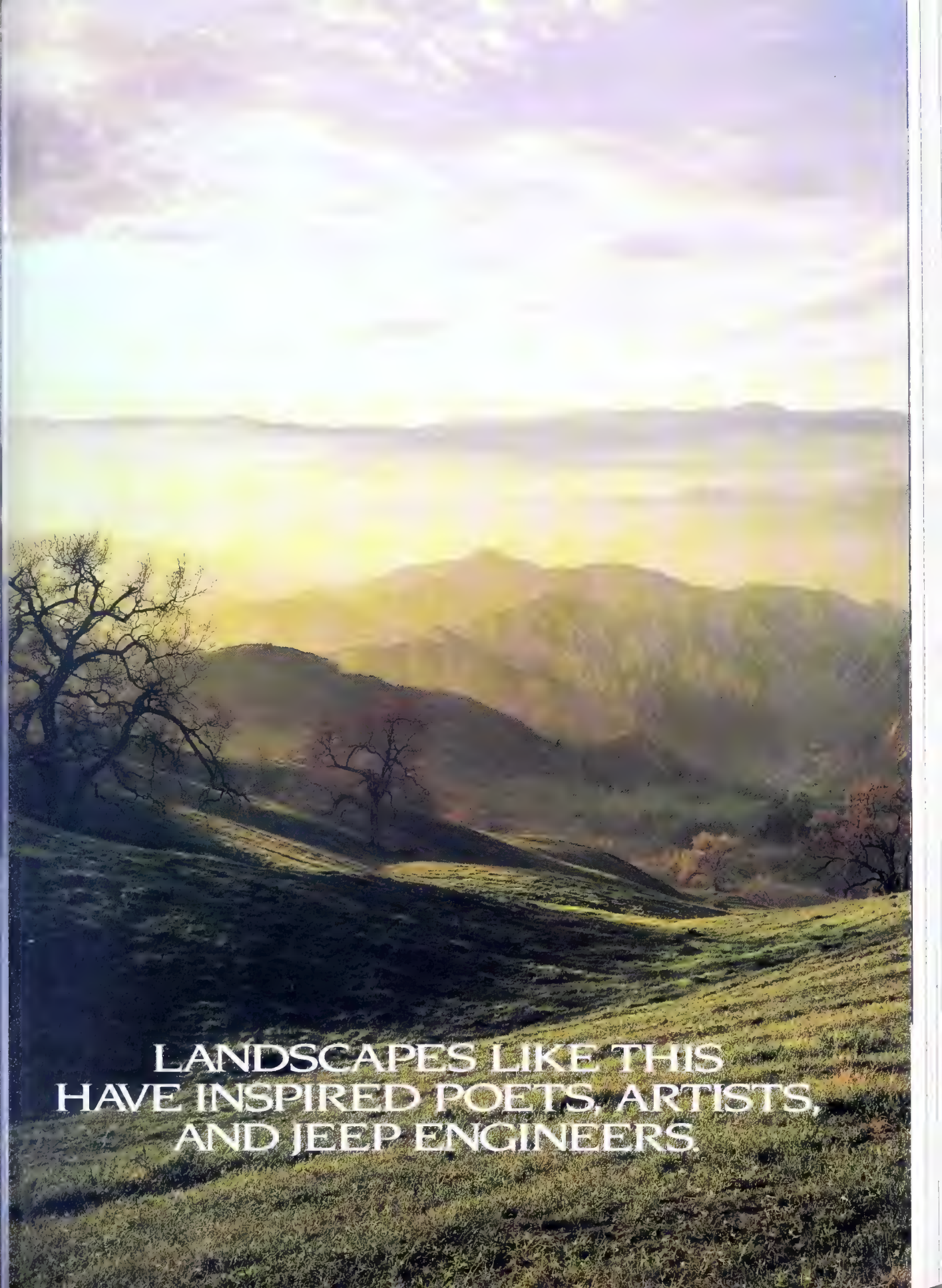
Zil has been turning out the same model for 30 years. But modernization will cost \$200 million

the modernization. Yet one outside investor, an aggressive Moscow financial company called Microdin that holds 18% of Zil stock, is balking because its ownership share would be diluted. It also wants Zil's management change before it puts in more money. Zil managers want

Yeltsin to replace Microdin and other troublesome investors with more "patriotic" ones.

As the corporate battles play out in coming weeks, investors will see whether such stories are hiccups on the way to a functional system of corporate governance or whether chaos and arbitrariness remain the norm. The health of Russia's economy rests on the outcome.

By Peter Galuszka and Patricia Kranz in Moscow

A full-page landscape photograph showing rolling hills under a dramatic, cloudy sky at sunrise or sunset. The sun is low on the horizon, creating a warm, golden glow that filters through the clouds and illuminates the hills. In the foreground, a large, dark, leafless tree stands on the left, and another smaller one is visible further back on a hill. The hills are covered in low-lying vegetation, possibly grass or shrubs. The overall mood is serene and majestic.

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AND JEEP ENGINEERS.

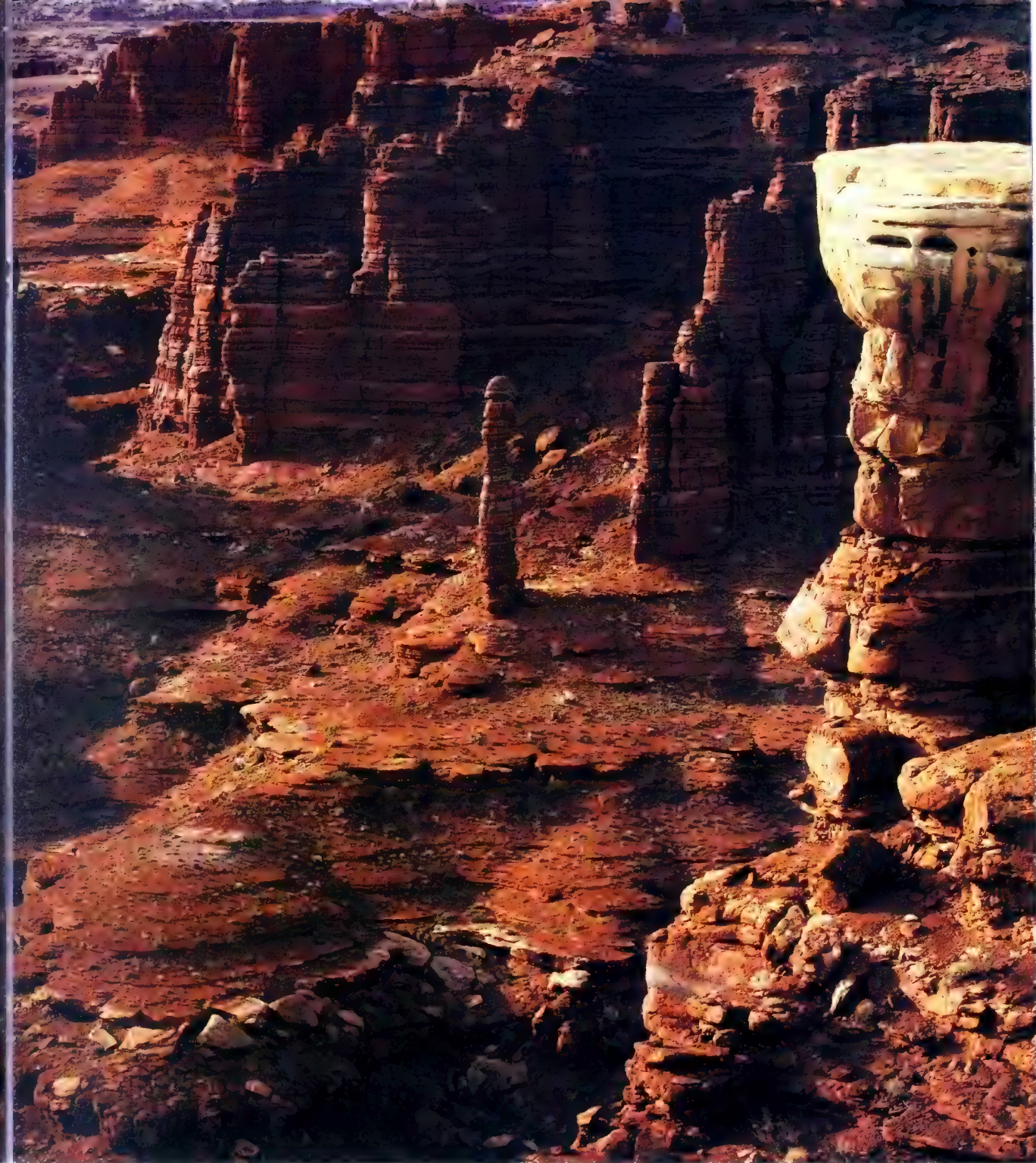
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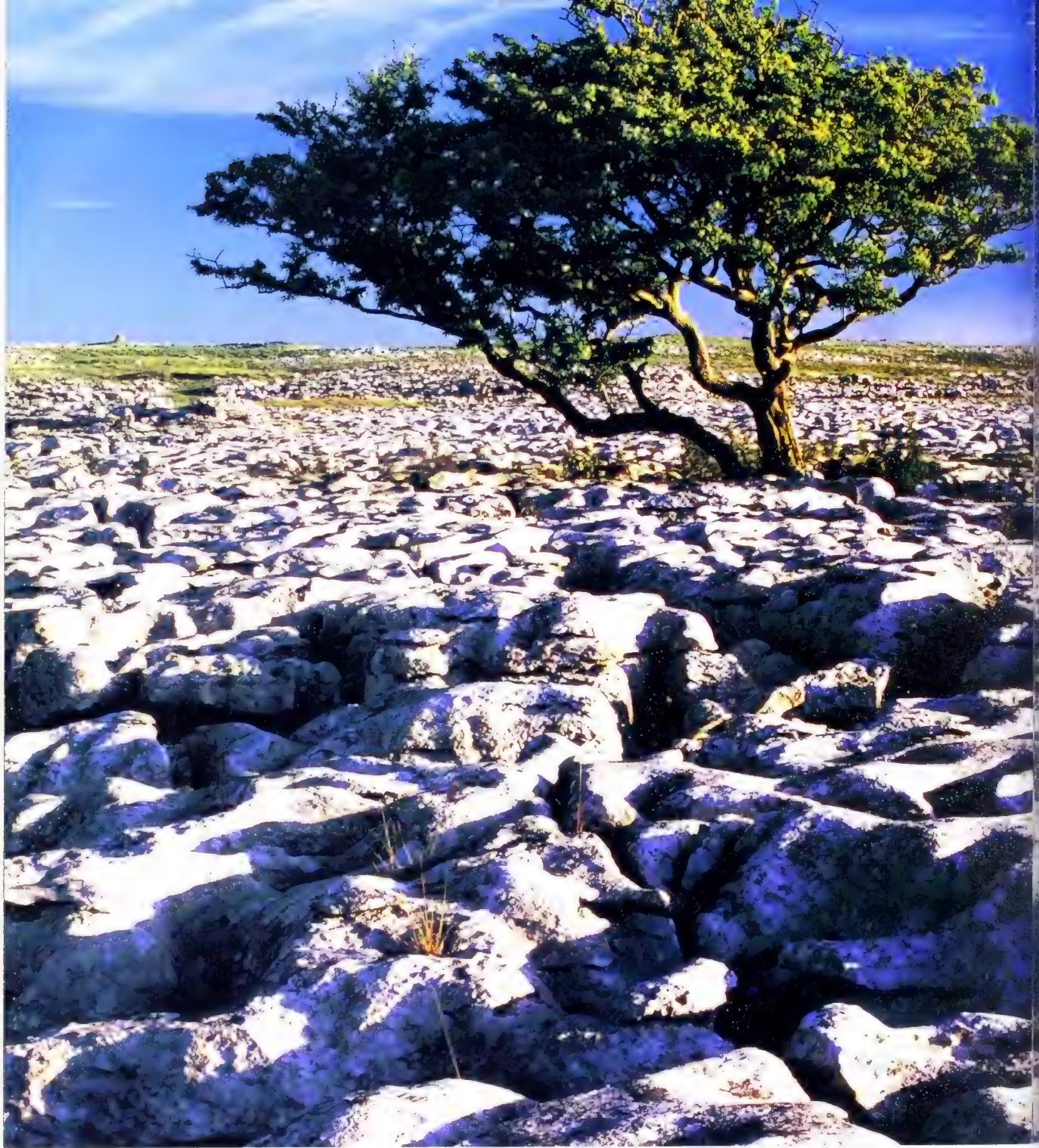
Of course, as any Jeep engineer can tell you, impressive specs don't mean much unless you've got the technology to convert them into usable traction.

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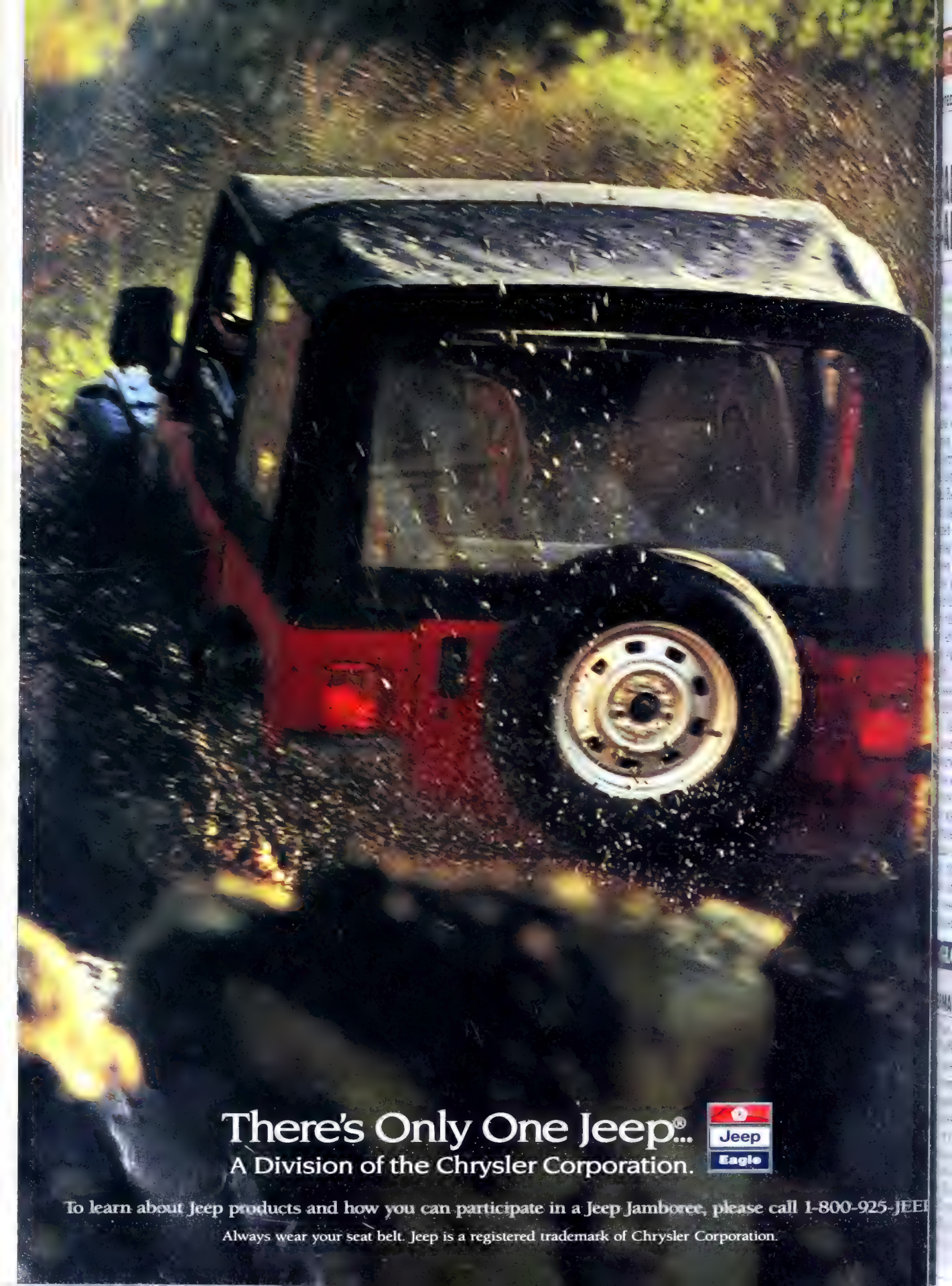


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AN ZEDILLO PUSH DEMOCRACY AND KEEP THE LID ON?

The debate rages in Mexican cafés, taxicabs, and corporate boardrooms: Many people say President Ernesto Zedillo Ponce de León is the weakest, most pathetic leader in Mexico's post-revolutionary history. But others defend him as a determined to deliver long-awaited democracy to his country.

While Zedillo badly fumbled the peso crisis, he is proving much more democratic leader than his predecessor, Carlos Salinas de Gortari. Zedillo has brought a member of the opposition into his Cabinet and ordered a sweeping remake of the corrupt justice system. He has also begun to curb the dictatorial power of his own Institutional Revolutionary Party (PRI).

In the short term, such moves have invited criticism. But the question is whether Zedillo is digging himself into an even deeper hole. By cracking down on the PRI, which has long kept Mexico in line, he could be crimping his ability to manage the country's troubled economy. And he may be opening the way to an explosion of protest over social inequality, supposed U.S. interference, and losses resulting from privatizations.

Zedillo's advisers are pondering these questions as they try to win back investor confidence and begin turning the economy around. They are planning to maintain strict fiscal and monetary discipline and hold the line on inflation. They want to move quickly on privatization—to raise money and reassure investors on Mexico's direction. "We've lost 90% of the credibility we built up over the last six years," says one senior government official. "We want to send a clear signal that the Mexican government means business."

But the inner circle is also hotly debating how much of orthodox Mexicans will swallow. They know there is a deep resentment over Mexico's pledging its oil revenues as collateral for the \$50 billion U.S.-led bailout and suspicion

of secret conditions on such issues as drug trafficking and immigration.

The government's plans to sell off railroads, power plants, and petrochemical units are already drawing flak from the PRI, including Zedillo's own Energy Secretary. That is not surprising, since these state industries have long been used to provide cushy executive posts for PRI higher-ups, as well as tens of thousands of jobs for the party ranks.

WIDER TROUBLE. Resistance is also stiffening from the normally compliant PRI-backed unions, which fear that privatization will bring massive layoffs. In recent weeks, angry oil

workers have blocked fuel deliveries to gas stations in Tabasco state. Unrest could escalate quickly as the predicted 1.5% decline in gross national product this year begins to bite and inflation soars to 25% or more. Workers are already chafing at the 7% wage ceiling the government wants. In what could presage wider trouble from long-quiescent Mexican labor, some 5,000 workers at a Thomson Consumer Electronics TV components plant in Ciudad Juárez recently struck for a week, forcing the shutdown of

Thomson's main U.S. television plant. They wrangled a 20% settlement that could undermine the government's anti-inflation efforts if other workers demand similar treatment.

Several upcoming state elections, such as one in Jalisco state, could also pose big problems for Zedillo. If, as expected, the center-right National Action Party (PAN) wins, PRI stalwarts could go on the rampage as they did a few weeks ago in Tabasco state, when Zedillo caved in to demands for new elections after a fraud-tainted PRI victory.

So the bailout is unlikely to end Mexico's troubles. Zedillo is arranging a demanding agenda for himself. And he hasn't proved he is up to it.

By Geri Smith in Mexico City



ZEDILLO: *Infuriating his own party*

GLOBAL WRAPUP

GERMAN PHONE MAN HANGS UP

After a storm of criticism, Gerhard Pfeiffermann has withdrawn from the supervisory board of Deutsche Telekom. The move is a victory for companies such as BellSouth, Cable & Wireless, and Veba that hope to break into or expand their activities in the German telecom business.

Posts and Telecommunications Minister Wolfgang Bötsch had appointed Pfeiffermann, one of his top aides at the Ministry, to the Telekom board about a month ago. But both German

and foreign industry cried foul, arguing that Pfeiffermann would be in the bizarre position of ruling on applications to compete against the state-controlled monopoly while sitting on its board. Bötsch at first insisted he saw no conflict of interest but finally yielded. Competitors hope that having won this victory, they can also force Bötsch to speed up Germany's painfully slow phone deregulation.

WHITE KNIGHT FOR WELLCOME?

► Most analysts figured Glaxo Holdings PLC's \$14.6 billion hostile take-

over bid for drugmaker Wellcome PLC wouldn't be topped, but some are rethinking. Wellcome's 1994 earnings jumped 19%, to \$1.1 billion, making it one of the industry's most attractive companies, with a 31.5% profit margin. But Glaxo's half-year results, released a week later, were less than sparkling, with a 10% earnings jump on a 2% sales rise. Now London analysts say Wellcome's figures may attract a white knight, with speculation focused on Pfizer, Roche, Bristol-Myers Squibb, Eli Lilly, and Johnson & Johnson.

"Did the weatherman say anything about solar winds tonight?"

It wasn't a rainstorm that knocked out the power in Quebec, Canada, and disrupted service in seven states in March 1989. It was the sun.

In addition to light and heat, the sun radiates an electrically charged gas called plasma, or solar wind. When the solar wind penetrates the Earth's magnetic field, it creates spectacular light shows known as the Northern and Southern Lights.

It can also create havoc.

Solar wind has disrupted radio communications, navigation systems and, as it did in March 1989, caused a massive power blackout.

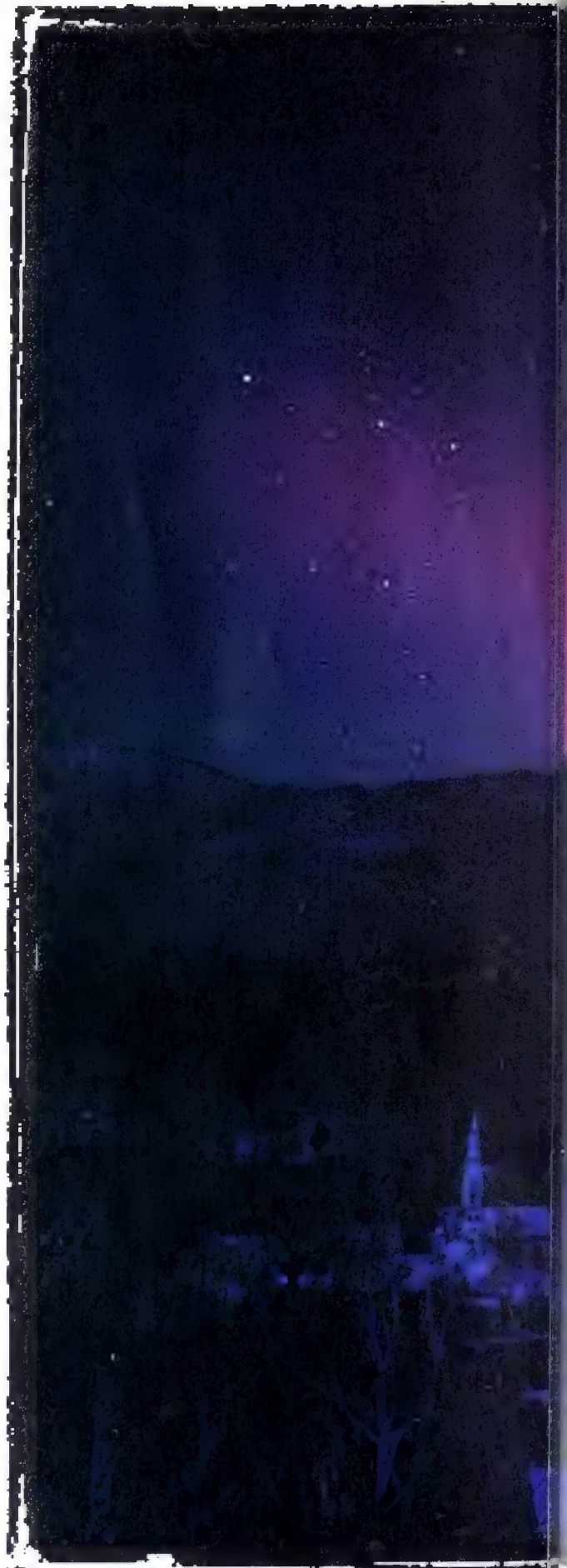
To help predict these potentially dangerous "space weather" conditions, NASA launched the Wind satellite on November 1, 1994. The first of two spacecraft in NASA's Global Geospace Science program, and part of an international satellite network, Wind will study the mass, momentum and energy of the solar wind for the next three years.

The data it sends back will provide the early warning needed to minimize solar wind damage to radar, microelectronics and the power supplies of entire cities.

As the company that designed and built Wind, which already is providing useful data to scientists, Martin Marietta is proud to be a part of the extraordinary NASA and Goddard Space Flight Center team.

What they learn in space today will safeguard the quality of life on Earth tomorrow.

MARTIN MARIETTA







WARNER HOME VIDEO'S
NEGOTIATING TEAM:
COOKSON, LIEBERFARB,
KING, AND OSTROVER

STRATEGIES

VIDEO WARFARE: HOW TOSHIBA TOOK THE HIGH GROUND

Suddenly, the disk developed with Time Warner is the one to beat

Koji Hase, a senior manager at Toshiba Corp., spent Good Friday of 1992 with Warren N. Lieberfarb, head of Warner Home Video Inc., brainstorming about how to cram full-length movies onto CD-size disks. Then, the two headed to Hollywood power restaurant Morton's for dinner. The soft-spoken Hase decided this brash, animated New Yorker reminded him of the Tasmanian Devil, Warner's voracious, whirling Looney Toons character. A few bottles of red wine later, they decided they both looked like the Tasmanian Devil. So when it came time in November to christen the project, Lieberfarb suggested "Taz," and the name stuck.

Now, the name is looking apt. Toshiba

and Time Warner Inc.'s double-sided, digital videodisk (DVD) has spun its way into the hearts of Hollywood movie moguls, while a rival system from Sony Corp. and Philips Electronics could get left in the dust. Toshiba's standard wowed Hollywood with 5 gigabytes of capacity per side, room for 135 minutes of high-quality video plus a host of interactive goodies such as viewers' choice of endings. The Beverly Hills unveiling was an awesome display of corporate clout. Movie powerhouses such as Warner Bros., MCA, and MGM/UA shared the podium with manufacturing giants Matsushita, Thomson, and Pioneer. The rival team isn't admitting defeat. But it's clear that Toshiba/Time Warner have won an early, important battle.

KEY ALLIES. How things turned out this way is one of the oddest tales to emerge from the struggle between Hollywood and Silicon Valley to dominate the dawning Multimedia Age. With an eye toward the Infobahn, the entertain-

ment industry wants a say in the standards that control the delivery of digital pictures into the home. Since Toshiba is ascendant in Hollywood, Sony and Philips have set their sights on computer makers, pitching their format as a high-density replacement for CD-ROM. That may drive an even deeper wedge between the two industries and spark an all-out standards war that would mire the new market in confusion.

Such a conflagration, if it comes at all, is probably months away. In the meantime, Toshiba/Time Warner's Hollywood victory holds crucial lessons for how multimedia deals get done. Rather than trying to dominate the new videodisk format with its own, patented technology, Toshiba, which owns a large stake in Time Warner entertainment, skillfully mediated among fractious competitors and stitched together an alliance that will be difficult for anyone to unseat.

The stakes are huge. DVD could blow som into a \$30 billion market by the

ly 21st century, predict ne members of the Toshi- camp, rivaling the VCR lustry today. For start- , there are the disk play- s, which Toshiba and its ies want to launch by d-1996 for about \$500. en, there's revenue from lions of disks Hollywood es to sell to consumers about \$20 a pop. Better still, the DVD sys- n could grow in many di- tions. Cable companies ld store DVD movies in deo jukeboxes," deliver- films over cable into bscribers' homes. Like ilips/Sony, Toshiba will o try to position its DVDS next-generation CD-ROM drives PCs and even merge them with next- generation game machines.

Toshiba moved the DVD project into h gear in June, 1993, deploying 100 ineers to work under semiconductor eran Taizo Nishimuro, Hase, and ashi Yamada. Building on technolo- developed with Matsushita Electric lustrial Co., the team found a way record billions of bits of music, vid- and text onto superslim disks just millimeters thick. The thinner lay- allow lasers to read smaller pits resenting digital zeros and ones, sting capacity far above that of con- tional music disks and CD-ROMs. o slim disks are then glued back-to- k to double storage space.

Technology in hand, Toshiba and Time rner tried to round up es among hardware mak- . Toshiba showed an ear- prototype to Philips in uary, 1994. But the tall, tely Nishimuro says lyps' response was "fuz- ' No wonder. Philips and y had pioneered the au- CD revolution 14 years lier and together had ex- ded it into CD-ROMs. They watched CD systems ex- d to an installed base of rly 100 million, with 3 ion disks in circulation. e future of higher-density ss, they figured, belonged hem.

A MUTINY. Matsushita was o entranced by the poten- of the Sony/Philips alli- e. Despite its work with hiba on the double-sided s, the Osaka-based giant ged its bets, helping y with its approach. y and Philips had even

WHAT TOSHIBA AND TIME WARNER DID RIGHT

- Pushed the technology envelope to 10 billion bytes of storage
- Courted Hollywood aggressively through ad hoc advisory group
- Placed films and games over computer applications
- Wooed other electronics companies with "open" licensing approach

WHAT SONY AND PHILIPS DID WRONG

- Slow to develop high-capacity digital videodisk prototype
- Sacrificed capacity for compatibility with existing disks
- Presented Hollywood with finished specs, instead of seeking advice
- Boasted of future recording capability, raising Hollywood copyright fears

Lessons from the trenches

hatched plans in April to announce a world standard with Matsushita.

Chances are the announcement would have gone ahead. But Matsushita's U.S. movie arm, MCA Inc., refused to get on board with Sony. Publicly, MCA said it would follow its Japanese parent. Behind the scenes, though, Matsushita's own technical-liaison people at MCA enlisted Warner's Lieberfarb to visit Matsushita headquarters and fend off a joint announcement with Sony.

The plea from MCA was a huge coup

for Toshiba/Time Warner. But Matsushita, the powerful maker of Panasonic and Quasar brands, continued to sit on the fence. Lieberfarb and his team—Christopher J. Cookson, Lewis S. Ostrover, Marsha K. King, and Joseph Vayda—realized they would need maximum support in Hollywood to stop Sony and Philips. He quietly organized an ad hoc committee of seven studios, chaired by Walt Disney Co.'s Robert E. Lambert and Richard B. Cohen, president of MGM/UA Home Entertainment.

"WE'VE GOT IT." The committee was a brilliant stroke that ultimately turned the battle in Toshiba's favor. In August, Sony toured Hollywood with a prototype that met with a tepid response.

A month later, the ad hoc studio committee released a wish list that played straight into Toshiba's hands. They wanted 135 minutes of playing time, high image and audio quality, and room for at least three languages, plus a parental "lockout" feature to skip over violent or risqué scenes. As Goldman, Sachs & Co. electronics analyst Eric Gan in Tokyo points out, a two-hour action movie, such as *In the Line of Fire*, eats up over 3½ gigabytes, largely filling Sony's disk and leaving precious little room for interactive applications. But Toshiba's 10-giga-byte prototype had room to spare. "I thought: 'This is it. We've got it,'" recalls Toshiba's Hase.

Philips and Sony continue to stress their technology's compatibility with current CD-ROMs. The new disk players can't just be a replacement for VCRs, insists Philips Consumer Electronics Program Manager Jacques Heemskerck, but the machines must also satisfy computer makers. Sony also questions the intense focus on Hollywood. Complains Managing Director Nobuyuki Idei: "I don't understand why the studios should be committed long before there is even a product."

In the end, Sony and Philips barged ahead with an official unveiling on Dec. 16, but they went to the podium without allies. Sony felt Toshiba's double-sided format would be too expensive for manufacturers. But just three days after the unveiling, Matsushita's DVD di-

DEJA VU? Eighteen years ago, when RCA cast its lot with the VHS standard, it boded ill for Sony's Beta. Now, RCA backs Toshiba's DVD



TOSHIBA'S YAMADA AND HASE WITH THE TEAM THAT DEVELOPED DVD

rector, Sakon Nagasaki, visited Warner Music's Pennsylvania disk-stamping unit, WEA Manufacturing, which had been test-producing double-sided disks for six months. Nagasaki came away convinced that Sony was wrong.

Two weeks after Nagasaki's trip, Matsushita cast its lot with Toshiba/Time Warner, followed quickly by Thomson, with its powerful RCA brand. RCA's consumer-marketing clout in the U.S., backing the VHS VCR standard, hastened the decline of Sony's Beta players 18 years ago. "We plan to spend as much if not more on DVD as we did on DSS," the company's wildly popular Digital Satellite System, says Joseph P. Clayton, executive vice-president of Thomson Consumer Electronics in Indianapolis.

FENCE-SITTERS. Even with Matsushita and RCA behind them, Toshiba/Time Warner can't declare victory. In Hollywood, several studios continue to bide their time. Fox Inc. remains uncommitted, as does Disney. But both could use the extra capacity from Toshiba's system. Disney's cash-cow animation eats up gobs of digital real estate.

Silicon Valley, meanwhile, isn't taking sides. But it's hard to see why computer makers would choose Sony and Philips. The two have shown that they can raise double-disk capacity to 7.4 gigabytes using a dual-layer technology created by 3M. Even so, that's much less than Toshiba's two-sided system. And 3M's dual-layer approach requires an extra manufacturing step, which means higher costs for disk-stampers.

For Toshiba and Time Warner, bringing Sony and Philips into the fold will require some of the trickiest negotiations either has ever faced. Already, to reel in Hitachi, Matsushita, and Pioneer, the pair had to make many compromises, incorporating bits of rivals' patented technology, which means sharing license revenues. They've wooed disk-stamping companies with similar promises of license flexibility. What's more, at \$500 per unit, the DVD players won't earn Toshiba much profit. So there is little room for Toshiba to make concessions to Sony, such as incorporating some of Sony's technology in the new standard.

There may still be time to forge a compromise. "We're only 500 meters into the marathon," says Sony's Idei. But over at Toshiba, Nishimuro's office boasts a trophy: a colorful, five-inch statue of the Tasmanian Devil that Lieberfarb sent him. Toshiba and Time Warner may not devour their rivals, but they've certainly taken a healthy bite.

By Larry Holmbeck in Tokyo and Larry Armstrong in Los Angeles

STRATEGIES

NOT SO SWEET TIMES AT HONEYWELL

In the dumps for years, it could find itself on the block

Take a tour of Honeywell Inc.'s giant factory in Golden Valley, Minn., and you'll see some of the most advanced production technology around. Sophisticated robots assemble parts for the company's home- and building-control systems, each doing work once performed by several people. Yet alongside those robots, high-priced workers assemble small batches of thermometers by hand, laboring over tasks now typically done in low-wage countries. And nearby racks hold copious amounts of inventory—a sight not seen in state-of-the-art factories for years.

Contradictions? You bet. For years, Honeywell has embodied more than its share. The Minneapolis-based company is a world leader in industrial controls, yet technical prowess hasn't translated to the bottom line. Honeywell has been in decline for a decade, and 1994 was no exception (chart). Net income slid 13%, to \$279 million, on revenues of \$6.06 billion, up 1.7%. Repeated downsizing hasn't helped: 1994's \$38 million write-off was Honeywell's sixth restructuring in eight years. Says a frustrated shareholder: "Sometimes I wonder if management knows what it's doing."

HIGH PRESSURE. Now time may be running out. Investors are growing impatient, and the board is upping pressure to show results. If Honeywell doesn't improve, it could end up on the block. Acknowledges CEO Michael R. Bonsignore: "We have to deliver."

Bonsignore—a 25-year Honeywell veteran who won the top spot in 1993—has promised Honeywell will hike profits between 12% and 16% in 1995, with double-digit gains the next two years. And he pledged that 1994's write-off will be the last. But investors, tired of Honeywell's promises that the payoff from restructuring is coming, appear unconvinced. Neither Bonsignore's upbeat tone—nor a \$600 million stock buyback—



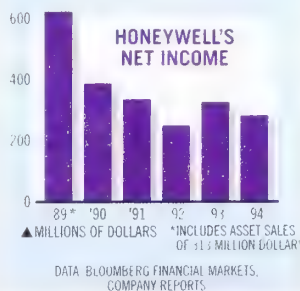
have bugged Honeywell's stock from the mid-30s range since 1992. Not even the recent dismissal of a \$1.2 billion judgment that Honeywell was to pay to Litton Industries Inc. for patent infringement boosted the stock.

Certainly, there's reason for skepticism: Honeywell hasn't seen double-digit growth for years. Bonsignore argues that the company has done as well as possible, given faltering markets. Space and aviation revenues nosedived from \$2.1 billion in 1991 to \$1.43 billion last year

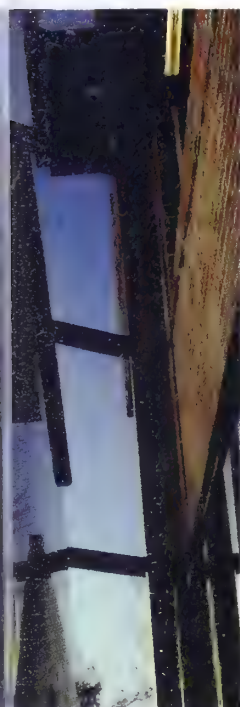
largely because of a slump at Boeing Co. Recession also dented Honeywell's home- and building-controls and industrial automation units.

Even so, rivals such as Emerson Electric Co. and Rockwell Intl. Corp. do far better in the same markets. In home air conditioning products, Honeywell's 10% operating margin falls well sho

AN EARNINGS SLIDE



Emerson's 15%, while Honeywell's 7% gain in aerospace is less than half the % earned by Rockwell. Critics say that's because Honeywell hasn't attacked costs aggressively enough. Although it has taken more than \$100 million in restructuring charges since 1986 to shrink manufacturing capacity and cut the workforce 28%, to 10,000 employees, the payoff has been small. Honeywell's sales, general, and administrative expenses ran 18% of sales in 1987, hardly down from 18.2% in 1987. Critics blame a clubby, paternalistic culture that avoids tough decisions.



STAGNANT

Why haven't repeated restructurings boosted the bottom line? Critics blame a clubby, paternalistic culture that avoids tough decisions

Explains one shareholder: "They could have taken \$500 million out of the company." Honeywell has only slowly moved labor-intensive jobs out of high-wage Minnesota plants, for example. And one executive adds that many laid-off workers slipped back on the payroll. "There's no discipline," he says. Honeywell has few outsiders in top management—and those who have come, including well-known cost-cutters such as Citicorp Vice-Chairman Christopher J. Steffen and William L. Trubeck, Southwest Airlines Inc.'s former CFO, haven't lasted long. Insiders say frustration with the slow pace of change is a key factor in their leaving.

Bonsignore argues that having long-time Honeywell people at the helm is a strength. "We know the company and what it is capable of," he says. As for criticism that he's moving too

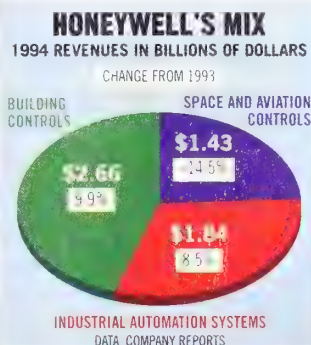
slowly, he says earlier moves to squeeze overhead and cut costs will soon pay off. And Bonsignore will finally trim Honeywell's top-heavy European unit in 1995. **FAT CONTRACTS.** He's also betting on rebounds in the company's major businesses. The end of recession in Europe and a strong replacement market in the U.S. should bring double-digit growth in home- and building controls. Ditto for industrial controls, which has nabbed big contracts in the Far East. Even the slide in aviation may be over.

But that may not be enough to keep Honeywell independent. One source close to the board says a number of outside directors have put senior management on notice. "They have to do well in 1995 or else," he says.

Still, others on the board are backing Bonsignore: "We are confident in his future leadership," says board member James Howard III, the CEO of Northern States Power Co. "There's no need to tear up this company." But without improvement, some large shareholders say they believe Honeywell could be ripe for a takeover, with General Electric, Siemens, and AlliedSignal mentioned as possible suitors. NatWest Securities Corp. analyst Nicholas P. Heymann says Honeywell could bring between \$46 and \$59 a share. Still, shareholders may have to wait. Takeover talk has surrounded the company since the late 1980s. And two years ago, GE formed a joint venture with Honeywell in industrial controls. One shareholder calls the GE deal "a wonderful poison pill." The logic: Even if GE doesn't want Honeywell, its presence keeps others from risking a bid.

Bonsignore says he fully expects to meet his growth targets. "I won't be satisfied with anything less," he says. And there are some signs of progress. At the Golden Valley facility, the racks of excess inventory will be gone by yearend. And those jobs being done by hand? They'll be moved if they can't be performed economically in Minnesota. But investors have heard this before. This time, Bonsignore knows he had better deliver.

By Kevin Kelly in Minneapolis



"To remain competitive into the next century, read this book!"

—Peter Lynch, Vice Chairman,
Fidelity Management and Research Company

THE DISCIPLINE OF MARKET LEADERS

CHOOSE YOUR CUSTOMERS,
NARROW YOUR FOCUS,
DOMINATE YOUR MARKET

**MICHAEL TREACY
& FRED WIERSEMA**

A new breed of company is reinventing the rules of competition — dominating its market by choosing one, and only one, of three values: best total cost, best product, or best total solution. To see how this powerful concept works at today's most successful companies, read *The Discipline of Market Leaders*, the book that sets the business agenda for the next decade.

"It's taken over a decade of struggle in the telecommunications market wars for AT&T to learn what is conveyed within the covers of this excellent book."

—Robert E. Allen, CEO, AT&T

ADDISON-WESLEY

HOW DELTA FLEW CIRCLES AROUND PAN AM IN COURT

The winner's legal strategists used every ploy in the book—and then some

Roy M. Cohn, the flamboyant lawyer best known as Senator Joseph R. McCarthy's henchman in the 1950s, once said: "I don't want to know what the law is. I want to know who the judge is." The comment is as crass today as it was then. But more and more, high-priced attorneys clashing over billions of dollars live by Cohn's advice. "I'm paid to win and to take advantage of the system," says New York defense lawyer Dennis E. Glazer of Davis Polk & Wardwell.

That's exactly what Glazer recently did. In a \$2.5 billion battle between airline titans Delta Air Lines Inc. and Pan Am Corp., Glazer spearheaded an elaborate three-year legal strategy for Delta that entailed everything from forum-shopping to investigating judges' backgrounds. These maneuvers were neither illegal nor unethical. They merely took advantage of an imperfect, malleable system, in the process costing Delta many millions of dollars for its bevy of lawyers. And for Delta, they delivered a stunning victory in December that saved the Atlanta-based carrier from life-threatening litigation.

TAKE THE EDGE. What makes the Delta case so noteworthy is the tidy way every element of the legal strategy fell into place. But similar high-stakes legal maneuvering goes on everywhere. Lawyers involved in hotly contested courtroom brawls look for any possible edge over their opponents. Cases ranging from product liability to the O.J. Simpson murder trial rely on costly scientific methods to refute evidence. Jury

consultants study how characteristics such as race and gender may affect a case. And lawyers search painstakingly for sympathetic legal forums. "There didn't used to be the pressures associated with losing that there are today," says Donald E. Vinson, a litigation-support expert. "Today these things are all a standard part of trial advocacy."

Standard, perhaps, to the practitioners. But few outsiders get to see just how the course is mapped out in a major corporate litigation, since many key decisions are made behind closed doors. The details of the Delta-Pan Am dispute, which have emerged through interviews and court records, offer a rare glimpse into how lawyers—within legal bounds—leave as little to chance as possible.

The Delta-Pan Am dispute first erupted in late 1991. Pan Am had been counting on Delta to help foot the bill for its comeback. But a \$1.7 billion deal soured that was to finance a new carrier, dubbed Pan Am 2, in exchange for Pan Am's profitable transatlantic routes and Northeast shuttle. Broke and grounded, Pan Am took the offensive and sued Delta for breach of contract. As the plaintiff, Pan Am could choose where to sue, and it picked the Bankruptcy Court for the Southern District of New York. The claim: that Delta's interest in the new venture was merely a ploy to capture Pan Am's best assets.

Counting on the generally pro-debtor stance of bankruptcy courts, Pan Am's lawyers didn't even bother to make the routine request for a jury trial. The judge handling the case, Cornelius

Blackshear, had even more going for him, they figured. He was already presiding over Pan Am's bankruptcy and was aware of the devastation the carrier's woes had brought to thousands of now-unemployed airline workers. As Blackshear's experience as a former New York City cop might make him sensitive to their plight. Blackshear declines comment.

But as much as Pan Am favored Blackshear, Delta opposed him. Recalls Glazer: "Our goal all along was to look for alternatives." That so much energy would be devoted to choosing venues isn't surprising. A study of federal cases from 1979 to 1991, which is to be published this fall, found that plaintiffs won early victories in 73% of the suits that remained in the court in which they were originally filed. In transferred cases, plaintiffs won just 26% of the time. "Transferring a case is a way of overcoming court bias," says study author Theodore Eisenberg of Cornell Law School. "There is room to manipulate the system."

MORALITY PLAYS. Delta also fought hard to avoid a jury. And with good reason. A jury consultant hired by Delta to conduct a series of mock trials found jurors especially susceptible to the emotional aspects of the case. The results were "mixed," says Glazer, but troubling enough to worry Delta.

Early in the case, Delta had argued against a move by Pan Am to consolidate the dispute before Blackshear with two other cases brought in New York district court by former Pan Am fil-

JANUARY, 1991 Pan Am files for bankruptcy in New York.

AUGUST, 1991 Delta agrees to a \$1.7 billion deal, which includes transfer of Pan Am's transatlantic routes and Northeast Shuttle. Delta

also proposes to form a new carrier dubbed Pan Am 2.

DECEMBER, 1991 Delta ceases all operations. Delta declines to pay millions, arguing that Pan Am's reorganization is doomed.



ALL-OUT WAR

“I’m paid to win and to take advantage of the system”

—DENNIS E. GLAZER



right to one. The issue remained unresolved until just days before the trial began, forcing the lawyers to prepare for two types of trials. Delta spent \$75,000 on more than 40 exhibits aimed solely at jurors. Pan Am also invested heavily in easy-to-read graphics. Those efforts were in vain when Patterson announced, to Delta's delight, that he alone would hear the case.

For more than five grueling weeks, the battle raged. And with every passing day,

it became clearer that Delta's instinct about Patterson had been right. Pan Am's 43 witnesses failed to persuade the judge. The witnesses included Pan Am's former CEO, Russell Ray, a portion of whose testimony Patterson termed "questionable." "In every instance, the judge took the slightest comment made by the other side and said it was right," fumes Pan Am creditors' committee attorney Leon C. Marcus.

NO APPEAL. When the time came for Delta to present its side of the case, it called only 15 witnesses. Delta's argument: That it had acted in good faith and that Pan Am's financial position had deteriorated so much from the time Delta had agreed to the \$1.7 billion deal that the reorganization plan was no longer workable.

Patterson agreed, issuing a stinging 209-page opinion on Dec. 22 that found virtually every factual question in Delta's favor. His decision boosted Delta's sagging stock price by four points the next day. "The judge went so far down the line on Delta's side that I can't even think, if I had done just one thing differently, the case would have gone our way," laments Pan Am's lawyer David E. Brodsky. On Jan. 10, Pan Am declined to appeal the ruling.

Delta's victory wasn't just the triumph of a clever game plan. The carrier also had a solid argument and some good luck. But Roy Cohn was definitely on to something.

By Linda Himelstein in New York

endants and pilots. Those cases were before juries. "Jurors tend to see as a morality play," explains Rob-S. Duboff, the consultant Delta l. "They decide morality by their standards, not by legalisms."

ckily for Delta, the cases were conated only for discovery purposes. airline employees' lawsuits landed e hands of District Court Judge rt P. Patterson Jr., a man whose League credentials and ability to ple with complex business matters hed the profile of Delta's ideal jurefore coming to the bench, he had ided companies as a partner in an e New York firm for 28 years. erson declines comment.

iving stumbled upon a judge they , Delta hatched a plan to get him. began filing motions before Paterson to gauge his interest in the airbusiness. That meant including in papers extra details about the ite and about the industry that t pique the judge's intellectual cu-

riosity. "We wanted to hook Patterson into the case," says Glazer. The idea was to make the judge want the case if the possibility arose.

Then Judge Blackshear handed Delta a gift. He told the lawyers that because of a crowded calendar, he would be unable to preside over the case. Delta didn't want to land in another bankruptcy courtroom. So it argued for consolidating the dispute with the former employees' cases pending in district court before Patterson—a 180-degree shift from its original position that the cases should not be joined. "Delta's change in litigation tactics smacks of forum shopping," complained Pan Am in court records. Nonetheless, in the name of efficiency, Patterson took the unusual step of pulling the case out of bankruptcy court and into his own. A trial was set for May, 1994.

Now, all that was left to decide was who would hear the case: a jury or Patterson. Since Pan Am hadn't initially demanded a jury, it lost its absolute

, 1992 Pan Am a in bankruptcy \$2.5 billion, alach of contract aith.

1992 Ex-Pan yees sue Delta illion, claiming 's refusal to

fund Pan Am 2 cost them jobs. A second employees' case is filed in September.

MAY, 1994 The trial begins before District Court Judge Robert Patterson Jr. and lasts for five weeks.

DECEMBER, 1994 Patterson rules overwhelmingly in Delta's favor.

JANUARY, 1995 Pan Am declines to appeal the case and pays back \$115 million it borrowed from Delta plus interest.

DATA BUSINESS WEEK

CAN YOU TRUST

Questionable sales tactics fueled by lavish incentives are prompting a rising tide of criticism

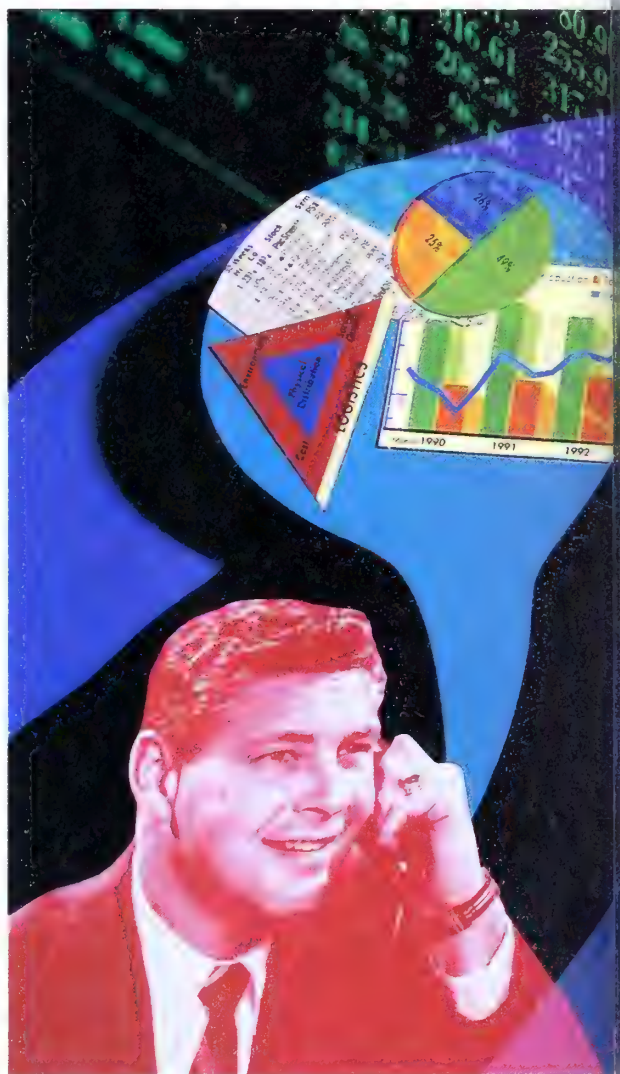
As a young, eager stockbroker in West Barnstable, Mass., in the mid-1980s, Caleb T. Warren spent hours charting companies' performance on yellow pads to find the best picks for his clients. One day, as he sat at his desk at Prudential-Bache Securities Inc., a manager grabbed a pencil out of Warren's hands and broke it. "That's for our research department," the manager barked before stalking off. "Your job is to sell."

Warren tried to take it in stride. But after stints at two other national brokerages, he just couldn't put up with the firms' unrelenting pressure to produce commissions, even though the investments often didn't benefit customers. In 1991, he formed his own money-management firm. He no longer collects commissions, instead charging his 70 clients a flat management fee. "I'm getting paid to make money for my clients, not to sell a product," he says.

Warren's views are part of a rising wave of criticism, both inside and outside the industry, of how stockbrokers and the firms they work for operate. For years, securities regulators have been concerned about shady penny-stock firms and so-called rogue brokers at larger firms. But now, critics are focusing on widely accepted ways of doing business at the biggest and most prestigious firms that they say systematically tend to put investors at a disadvantage. "There is a growing cynicism and suspicion among investors about the industry and its practices," says Arthur Levitt Jr., chairman of the Securities & Exchange Commission.

"UNSUITABLE PRODUCTS." This investor backlash stems in part from the limited-partnership scandals of the 1980s, especially at what is now called Prudential Securities Inc. Investor losses there exceeded \$1 billion. The abuses at Prudential Securities stemmed directly from sales practices and compensation systems that induced brokers to put clients into high-risk partnerships originated by the firm. Prudential Securities declined to be interviewed about their current practices.

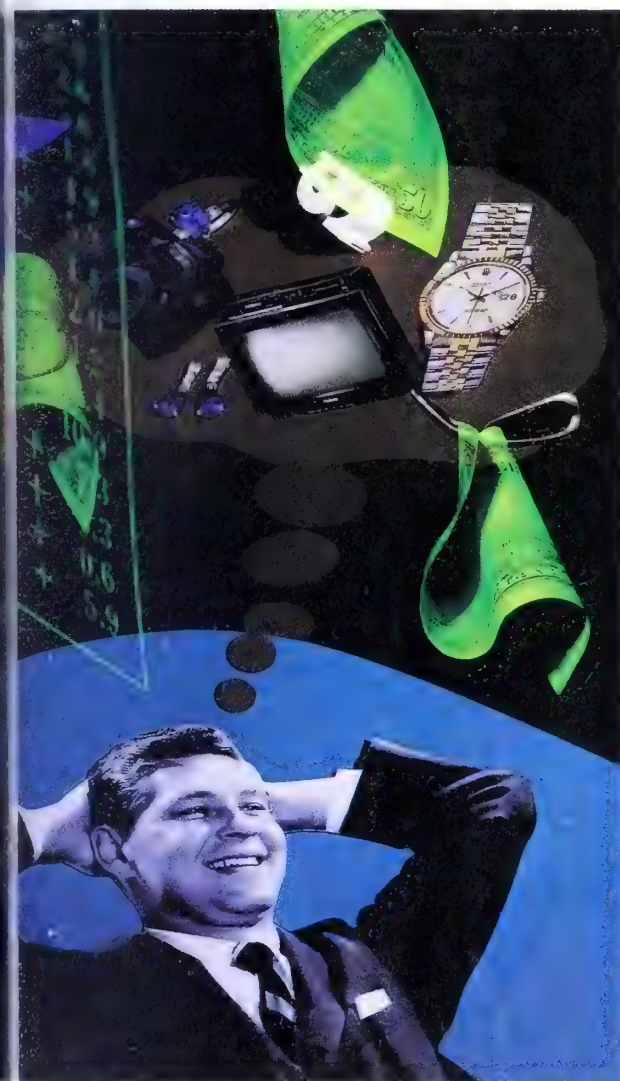
Today, products of major firms are generally less hazardous to customers' wealth. But ingrained commission compensation policies, which are at the very core of the way Wall Street does business, still tend to encourage brokers, who work almost entirely for commissions, to put their own interests ahead of their customers'. "Prudential showed us how sales contests and



paying higher commissions for in-house products led brokers to sell customers unsuitable products," says Idaho State Securities Commissioner Wayne Klein. "These sales techniques are still a serious problem that put the integrity of the industry at risk."

Many brokerage executives are increasingly worried that the industry is hurting itself. Commission incentives have been crucial to the industry's often lush profits and its broad high-cost array of investor services. But they are also undermining Wall Street's competitiveness. As the reputation of mainstream brokers plummets—one public-opinion poll found that only politicians and lawyers ranked lower—customers are leaving. So are disenchanted brokers such as Warren.

YOUR BROKER?



The Case Against The Brokerage Industry

PRESSURE The compensation system at brokerage firms creates intense pressure on brokers to generate a high volume of commissions.

INCENTIVES Brokers are given extra incentives, such as Rolex watches and all-expense-paid vacations, to sell special high-profit-margin products with little regard to their suitability for customers.

BAD ADVICE Firms push brokers to recommend in-house mutual funds, where the firm earns management fees, instead of funds run by outside managers. Most in-house funds have mediocre performance records.

BONUSES Many firms recruit top "producers" from other firms with huge up-front bonuses and extra-high commissions. That gives the producers an added incentive to promote excess trading.

POOR INFORMATION Firms don't provide customers information on the overall return on their investments and aggregate commissions they've been charged.

DATA BUSINESS WEEK

the commissions they can keep. That can encourage "churning," excessive trading of customer accounts. Sales contests and "product of the month" campaigns are common. Many firms recruit top-producing brokers from other firms with huge up-front bonuses, like star athletes. "How can that be in the interest of investors? It's a bad practice and should be eliminated," says Levitt. ■ Firms give little regard to whether customers benefit from investments. Brokers, for instance, receive financial incentives to push in-house products, such as mutual funds, instead of funds originated by outside groups. The reason: In-house investments produce higher profit margins. But these investments may be unsuitable or have worse performance records than products from outside vendors. "Customers are being told 'this is the best thing for you,' when the real reason is that the broker gets more money for it,"

the beneficiaries of this trend are discount brokers, directing mutual-fund groups, financial planners, and banks, whose employees mainly work on a fee or salary basis. The national full-service brokerage firms' share of securities industry revenues fell from 39% in 1992 to 35% in 1994, while discount brokers' share grew from 3% to 4%. "There is a lot at stake, and everybody in the industry knows it," says Samuel L. Johnson III, a professor at Harvard business school. Big firms know they must clean up their acts to salvage their niche. "Among the practices under scrutiny: commission incentives dominate and distort compensation. The more commissions brokers generate, the larger a share of

says Alan Bromberg, securities-law professor at Southern Methodist University.

■ Most firms provide little useful information to customers on how their investments are faring. Brokerage statements don't show an account's performance. And there is no disclosure of the aggregate commissions that a customer has paid over a quarter or a year. "If they started including performance and the cost of commissions on brokerage statements, the industry would disintegrate," says Howard G. Berg, a financial consultant and 30-year industry veteran.

Nothing is inherently wrong with commissions. Salespeople get paid on commission for selling everything from suits to

cars. In these cases, customers understand the salesperson's job is to sell a product. In the brokerage industry, too many naive customers forget this and trust their broker to do what's best for them. "Firms are deliberately trying to hide

Cover Story

the fact" that most brokers are simply salesmen, not financial consultants, says former broker Robert F. Mewshaw, now an investment adviser.

Brokerage executives dispute that the commission system induces brokers to work against clients. "You have to be stupid to make a trade purely because of what the commission is. If it's not in the customer's best interest, you're out of business," says John L. Steffens, who heads Merrill Lynch & Co.'s brokerage unit. Industry leaders say investors face far greater risks from penny-stock firms, inexperienced bank-based brokers, and unregulated advisers. Brokers, they note, are the most highly regulated financial-services providers.

No one disputes, further, that there are many good brokers who rise above the system. These brokers report rates of return to their clients and recommend the best investments. "I sell some PaineWebber products that are good products, and if they are not good, I don't sell them," says Howard Kramer, a veteran PaineWebber broker.

MORAL SUASION. Brokerages, however, are coming to understand that they have to change their ways. "People have to believe that the industry has its clients' interests at heart," says Steffens. "If they don't and a new entrant does, it won't be good for the industry." He concedes that such reforms as eliminating sales contests and extra commissions could cost revenues in the short run. "But in the long run, the impact will be positive in raising client confidence."

Last December, the industry launched a "trust and confidence campaign" to improve brokers' image. It has set up a new, continuing broker education program. Some firms are moving toward fee-based compensation and have stopped making brokers favor house brands. The most offensive contests have been toned down.

Levitt, a former broker, is spearheading the reform. He is relying on moral suasion, admittedly a tall order. Levitt has set up a high-level group to examine broker compensation practices, led by Merrill Chief Executive Daniel P. Tully, Warren E. Buffett, General Electric CEO John F. Welch Jr., and Harvard's Hayes. A report is expected within weeks.

It won't be easy to change the system, which is fundamentally skewed toward selling, not dispensing disinterested financial advice. Recruiters rank sales skill much higher than a college degree as a requirement for new brokers. Most training programs tend to impart little more than superficial financial knowledge. Florida investor James Leavengood says he has heard brokers admit they have no time to read the financial press. "Brokers are the nicest but most shallow people," he says.

The system richly rewards big pro-

In-House Mutual Funds: Bad Deal For Investors?

5-YEAR
RETURN*

INDEPENDENT FUND GROUP

Fidelity Group	64.9%
American Funds Group	50.8
Putnam Mutual Funds	47.7
Vanguard Group	47.3
Franklin Group of Funds	43.4

*Cumulative total returns, appreciations plus reinvestment of dividends and capital gains, for largest fund group

ducers. For example, in 1994 at Smith Barney Inc., a broker generating \$149,000 in commissions for the firm earns \$49,100 or a 33% "payout." But a broker with \$1 million in commissions earns \$425,000, a 42.5% payout. Managers encourage performance in other ways. One war story, in a National Endowment for Financial Education study, related how a branch manager asked a rookie broker for his shoes. He would own them back if he sold 10,000 shares of an automobile stock.

The incentive for brokers to produce is relentless. You

AT THE SEC, A DEFT CRUSADER FOR REFORM

Arthur Levitt Jr. isn't your typical Securities & Exchange Commission chairman. After an Aug. 8 meeting with Berkshire Hathaway Inc. Chairman Warren E. Buffett at his Omaha headquarters, Levitt waved off Buffett's offer to telephone a taxicab for the airport trip. Levitt and an aide figured they would hail a cab. But Omaha isn't Washington or New York—empty cabs don't fill the streets. So with time to kill before his flight, the 63-year-old Levitt walked the eight miles to Eppley Field airport. "I viewed it as an adventure," Levitt says.

The SEC chief is nothing if not a free spirit. And he has proved it often during his 18 months on the job. Despite his background as a liberal New York Democrat, he's no regulatory activist. And while he worked for decades on Wall Street, he doesn't hesitate to attack some of the securities industry's fundamental tenets, especially its conflict-of-interest-ridden system for compensating brokers. "Consumer protection is my mission and passion," he declares.

Levitt's pro-investor stance was shaped by his Depression-era parents: Arthur Sr., New York State comptroller for 24 years, and Dorothy, a career school teacher. As comptroller, Levitt's father managed one of the biggest pension systems in the country, and Levitt says his parents were "obsessive" about safely managing retirement savings.

That lesson guided Levitt's career in

the securities industry. As a broker in the 1960s, he was viewed as a skillful salesman but a straight shooter. He earned the nickname "Granny" for his sense of propriety. As president of Hayden Stone Inc., which became Shearson Lehman Brothers Inc., he advocated a salary-and-commission system for brokers instead of just commissions. But the notion went nowhere. "The leagues at the firm thought it was a haywire idea," he says.

Today, Levitt has a bully pulpit preaching his reform gospel. He's full of new rules but hopeful that his use of persuasion and ability to build consensus can produce voluntary change. He no longer favors a system that blends salaries and commissions. Industry leaders have persuaded him to propose fixed salaries on brokerage commissions could drive many of them out of business in down markets. Now, Levitt favors bonuses based on portfolio performance and still wants to abolish what he considers the worst abuses, such as excessively high commissions for sales of in-house products. "Arthur wants a better break for retail investors but not at the expense of straitjacketing the industry," says Harvard business school professor S. L. Hayes.

It's not clear, however, whether his drive to overhaul compensation will fare any better than some of his other crusades, such as a plan to

5-YEAR MORNINGSTAR
RETURN* RATING**

BROKERAGE FUNDS

ey	41.5%	3.1
r Funds	40.5	2.7
er Mutual Funds	40.2	2.3
ch Group	40.1	2.8
Securities	37.4	2.8

tings range
5 (best)

DATA. MORNINGSTAR INC

must train hundreds of new ones a year. Firms sustain the sales culture by doling out recognition perks. Fledgling brokers start out in a bullpen area and graduate to an office if their sales increase sufficiently. Biggest producers get secretaries and sales assistants. If open enough new accounts or generate big sales of certain products, brokers get to pick prizes, such as golf clubs, cameras, from glossy catalogs. A 1992 PaineWebber "premium producers" catalog explains how brokers can earn

brokers with few clients are especially vulnerable. Most brokers are ranked daily by commissions. At many firms, veterans who do not consistently bring in at least \$150,000 in annual commissions are quietly asked to leave. About 75% of new brokers don't make it in five years, which is why the big

credits for selling life-insurance products. Producers could earn a Rolex watch and a trip to Quebec, where "gala PaineWebber receptions and dinners fill the evenings in the grand style to which we have become accustomed." PaineWebber says it no longer has prize catalogs.

FANCY WEEKENDS. Most firms have chairman's and president's clubs, which reward the firm's top-producing brokers. They are often feted annually by top management at luxury resorts. In 1994, members of PaineWebber's Pacesetter's club—brokers who made at least \$350,000 in gross commissions—spent a weekend at the Phoenician in Phoenix serenaded by disco queen Donna Summer. "The firms hold carrots in front of brokers. The brokers get on the phone and hold carrots in front of the clients," says former Lehman Brothers Inc. broker Paul Warehall. Joseph J. Grano Jr., president of PaineWebber Inc., says the trips reward gross sales, not sales of particular products, and that brokers attend daily training sessions.

There are special enticements for certain high-margin products. One former PaineWebber broker won a trip to La Costa, Calif., in 1993 for selling \$1 million worth of PaineWebber's infamous U.S. Short-Term Government Fund, which subsequently lost as much as 9.3% of its value because of bad derivatives investments. PaineWebber says brokers could

"Consumer protection is my mission and passion"

ARTHUR LEVITT JR.

Chairman, Securities & Exchange Commission

the SEC's budget with fees on such things as stock registrations. The House passed such a bill last year with strong support from Democrats. But it died in the Senate because of opposition from Senator Phil Gramm (R-Tex.), who now chairs the subcommittee that oversees the SEC. Gramm wanted to maintain congressional control over SEC revenues. Levitt's intense lobbying alienated some senators, who branded him a "whiner," says an SEC official. "It was a no-win situation that Arthur never should have gotten involved with," he adds.

But on most issues, Levitt is proving that he is deft enough to maneuver in a Republican-dominated Washington. His emphasis on consumer education, investor self-reliance, and reducing regulatory burdens—especially for small business—plays well with the GOP. And since the election, the SEC has taken the unprecedented step of telling a court that a shareholder suit against Cooper Cos. had no merit. That decision dovetails with a provision in the Republicans' Contract With America that calls for limits on frivolous lawsuits by shareholders. "Levitt read the tea leaves early on," declares Barry Siegel, executive director of the Committee of Publicly Owned Companies, which lobbies for midsize firms.

In this hostile climate, Levitt, a consummate schmoozer, will push his agenda by forging compromises. He'll continue to meet not only with lawmakers but also with Wall Street officials and corporate chieftains. He'll be using up shoe leather in more ways than one. "I hope to walk to two or three more airports," he says with a smile.

By Michael Schroeder in Washington

earn the trip for selling \$1 million in any mutual fund.

Or consider a memo to Dean Witter Reynolds Inc. brokers in the Southeast region in October, 1994, announcing that brokers who sold \$50,000 in the Trust Company of the West/Dean Witter Global Convertible Trust would qualify for a week-

Cover Story

end in Bermuda. James Higgins, president of Dean Witter's brokerage unit, first denied the firm held single-product contests. When presented with a contest brochure, he conceded that the firm may have regional contests but insisted it had no national single-product sales contests. The fund is down 2.2% since October.

But the greatest incentives are usually for selling investments created by the firm. The reason for favoring its own products, especially mutual funds, is simple: much higher profit margins. The firm reaps a fee for managing its own funds. It gets no management fee for an outside fund. "The firm's product should sell because it is competitive, not because the firm gets a higher fee," says Idaho's Klein.

The firm that's most vulnerable on this issue is Dean Witter. It says that more than 75% of the mutual funds it sells are the house brand, probably the highest ratio in the industry. Customers who invest in Dean Witter funds pay a sales load that ostensibly compensates the broker for unbiased

advice in helping them pick the best fund. Yet three times of four, clients are simply ushered into Dean Witter funds. One reason: Brokers receive 5% to 15% more for selling Dean Witter funds than for outside funds. "It's like calling yourself a car consultant when you sell Fords," says Don Hips, publisher of *Morningstar Mutual Funds*.

If the performance of Dean Witter's funds was top-notch, such a bias might be justified. But Dean Witter's mutual-fund family, like most other brokerage-firm funds, is nothing special. The largest independent mutual-fund groups, such as Fidelity, Vanguard, American, Putnam, and Franklin, in general have better-performing funds (table, pages 72-73).

"PRETTY MEDIOCRE." The average Morningstar rating for Dean Witter fund is 2.72 stars out of 5 stars, placing it ninth out of the 10 largest independent and brokerage-fund families. According to Morningstar, the annual return of Dean Witter U.S. equity funds going back to 1980 is just 8.9%, trailing Standard & Poor's 500-stock index by 5½ percentage points. Except for a few, "the Dean Witter funds are pretty mediocre," says Morningstar analyst Eileen Makoff.

Dean Witter, whose advertising tagline is "we measure success one investor at a time," responds that having control over the funds it sells allows it to ensure the funds' quality. Its efforts to educate its brokers about the virtues of its own funds are what boost sales, not higher commissions, insists Dean Witter's Higgins. "All things being equal, a

SHOOTING STRAIGHT—AND STRIKING IT RICH



"I'm not dialing for dollars or just writing a ticket"

JOHN OLSON

*Financial Consultant &
First VP of Investments
at Merrill Lynch*

When John D. Olson, 40, joined Merrill Lynch & Co., the tall, boyish former accountant from Price Waterhouse started at the bottom, making cold calls to get people to open up brokerage accounts. But he soon realized he didn't like pushing customers in order to produce the maximum volume of commissions. He preferred a more time-consuming but productive approach: sit-

ting down with clients, discussing their finances and goals, and coming up with an informal financial profile. This way, he could suggest appropriate investment strategies and build long-term relationships.

When Merrill in 1993 initiated a campaign to gradually transform the firm's commission-driven brokers into financial planners who earn a flat percentage of client's assets under

management, Olson eagerly signed on. He now can give clients elaborate 80-page plans. "It's a whole different mentality and mind-set. I'm not dialing for dollars or just writing a ticket," he says.

Olson's sharp focus on customers has paid off: He has \$325 million in customer assets. Olson—and Merrill—are a long way from phasing out commissions. Olson, whose wife is also a Merrill broker, still gets 75% of his compensation from commissions vs. 25% from a variety of flat fees based on assets under management. But the broker may be the wave of Merrill's future. "If I had 12,500 like him, our stock would be 300," says John L. Steffens, Merrill Lynch & Co.'s retail brokerage chief. Now, if Merrill could just figure out how to clone him.

ld like our customers and brokers to e a Dean Witter-first approach when omes to Dean Witter products." Smith Barney also favors its own ls in several ways. It doesn't pay ers extra commissions for selling ch Barney funds. But it does give an extra bonus. Smith Barney says bonus is modest and deferred for years. Branch managers, who are a percentage of the profits of their ches, must forfeit 21% of these prof- less more than half of the funds are proprietary. One former execu- says he knows of one manager who to forfeit \$60,000 in pay for not ing this goal. The firm confirms that ch managers are paid partly on in- e mutual-fund sales, but the method eulation has changed.

t the other extreme is St. Louis- d A.G. Edwards & Sons Inc., h has no in-house mutual funds. It ves brokers should be free to pick 's best for the client. Otherwise, Chairman Benjamin F. Edwards 'the brokers feel prostituted. They the promise of a higher payout the threat of disloyalty if they don't e company way."

ING EXPENSES. Concerns such as e don't always bother Wall Street's salespeople, who actively market selves on the basis of their produc- Nearly all the major securities pay hefty up-front bonuses to re- top-producing brokers. The lure is only their sales ability but their omers' assets, which they bring with them. In essence, the broker client assets as a bargaining chip himself. Brokers typically persuade ts to come along by saying the firm is somehow superior to the ne. They rarely tell clients the e truth—that they are leaving for cold hard cash.

g producers are also paid a higher commission percentage they join a new firm. The rationale is that these rs make up for the costs that brokers incur by moving. effect, however, is the broker has an even greater incen- to trade his accounts because of the higher commis- he will earn. Customers who follow their broker to er firm may lose in other ways. Moving their accounts incur fees and penalties, especially if a customer has to ate one in-house fund and buy into a new one. ineWebber and Prudential offer the highest up-front ents, say brokers and recruiters. Consider Pru's hiring of e Kramer, Smith Barney's Seattle branch manager, in According to former associates, Kramer in turn hired than 25 Smith Barney brokers from his old office, pay- s much as "70-50-50" for the best brokers. This means a n-dollar producer would get a \$700,000 cash payment to to the new firm, plus 50% of gross commissions earned e next 50 months. Kramer denies Pru paid that much. o says PaineWebber pays average up-front payments. e big New York firms say that they dislike up-front ents. But the practice is likely to grow as firms scramble id up assets. Merrill Lynch spent \$21 million in the quarter of 1994 alone on signing bonuses paid to bro-

A CHAMPION FOR AN EMBATTLED INDUSTRY

"The majority of brokers make the right decisions"

JOSEPH J. GRANO JR.

President of
PaineWebber Inc.



Joseph J. Grano Jr. is among the most vocal defenders of the industry. "The major firms have never been cleaner," he says. "The majority of brokers make the right decisions for the right reasons." But that isn't stopping the former Green Beret from promoting improvements. As recent chairman of the National Association of Securities Dealers, he

pushed for continuing education for brokers. He has backed PaineWebber's state-of-the-art broker terminals, a big step in getting more information to clients. He also favors more disclosure to customers of brokerage firms' compensation policies. These steps would benefit an industry whose image, he acknowledges, "has never been worse."

kers hired in that quarter. Merrill says this was the most it had ever paid in a quarter and stemmed from an effort to hire Kidder, Peabody & Co. and Lehman Brothers brokers.

Customers are oblivious to this high-stakes competition. They are also often oblivious to whether their brokers are doing a good job for them. Brokerage statements at major firms don't show rate of return on a percentage basis. Nor do statements report the total amount of commissions paid per year, even though brokers have a running tally on their computer screens. Commissions, if they are disclosed at all, are reported only on a per-trade basis.

The public's disenchantment with stockbrokers, coupled with intensifying rivalry among firms to be more customer-friendly, is producing some reforms. Chicago-based William Blair & Co. is in the final stages of giving its brokers separate customer statements with rate-of-return information, which brokers can pass on to clients. "We think there are customers who want that," says a Blair official. Merrill is several months away from rolling out a new statement to some customers that will include rate-of-return data for stocks, bonds, and cash. No firm interviewed by BUSINESS WEEK has plans to report aggregate commissions, however.

Merrill Lynch, Smith Barney, and PaineWebber say they no longer pay brokers a higher commission for selling house-

brand funds. "I know my proprietary sales went down when we removed the differential," says PaineWebber's Grano. "That tells you there was a bias." These firms also deny they have sales contests for specific products.

Cover Story

While commissions still dominate, a small but growing part of big firms' business is fee-based, removing the broker's incentive to churn accounts. Brokers can earn a quarterly fee for referring customers to an outside money manager, called a wrap account. But this is not a panacea. The charges are high, with the customer paying annual fees as large as 3%.

Levitt is determined to make sure the industry keeps moving in the right direction. Under the auspices of the Tully commission, he has been meeting with the heads of the major brokerages. At least publicly, industry honchos praise his efforts. "I came away feeling good. The industry should always work at improving itself," says James Dimon, Smith Barney's chief operating officer. The Tully commission report is expected to implicitly criticize certain practices by lauding firms for not engaging in them, including contests for specific products, high payments to recruit brokers, and differential payments for in-house vs. outside products. If the industry doesn't curb the most egregious practices, the SEC may step in and require firms to inform customers of brokers' incentives. "Full disclosure is the most likely remedy we'll see implemented," says Harvard's Hayes.

In weighing whether to maintain commission incentives, big firms are between a rock and a hard place. If they keep the current system, they could lose market share. But if they move toward a fee system, they might lose major revenues since brokers would be less production-oriented. Whether ex-

ecutives can transform

"commission junkies," as former broker Mewshaw calls them, into trusted financial advisers could determine whether the industry prospers or slips into a slow decline.

By Leah Nathans Spiro in New York and Michael Schroeder in Washington

America Online users can chat with the authors on Sunday, Feb. 12, at 9 p.m. EST in a BUSINESS WEEK Online conference.

HOW ONE NEST EGG GOT SCRAMBLED

Jennifer Josephs has learned about investing the hard way. Back in 1988, she reaped more than \$1 million from the sale of some Las Vegas property. She sank about \$800,000 into a stock portfolio. Six years and four brokers later, her nest egg is worth about \$370,000.

Why the poor record? She charges, and her trading records suggest, that four separate brokers excessively traded her account, often in risky investments, and made trades without approval. "I was ripe for the picking—someone with a lot of money and no experience," says Josephs, 44, who owns a successful real estate development and management firm in Las Vegas.

Naïveté was her undoing. After she agreed to let a Shearson Lehman Brothers Inc. broker trade on her behalf, the broker made \$100,000 worth of stock purchases against her wishes. Her brokers also made big trades on margin, max-



"I was ripe for the picking—someone with a lot of money and no experience"

JENNIFER JOSEPHS

Burned Investor

imizing commissions and interest income for the firms. In 1992, for instance, Josephs paid trading commissions of \$20,134 and margin interest of \$18,124. Her profits on all of this trading: \$2,153. Smith Barney, which bought Shearson, declined to comment.

To avoid such hefty commissions, Josephs switched to a discount brokerage house. However, her new broker soon started trading excessively—and without authorization—in over-the-counter stocks in which the firm was a market maker. For instance, the broker bought \$120,000 worth of two stocks without Josephs' authorization, and they are down an average of 30%. Having lost one arbitration against a brokerage firm, she has been too discouraged to file any new complaints. "The more you have, the more they take advantage of you," she believes. Today, Josephs is wise but a lot less rich.

Recognition for Premium Producers

GOLD-PLATED CARROT
PAINEWEBBER PRIZES
AND A DEAN WITH
SALES-CONTEST FLOWERS

Atlantic Region 6

**TCW/DW CONVERTIBLE VALUE
AE SALES PROMOTION**

October's featured fund offering is the TCW/DW Global Convertible Trust. With assets exceeding \$100 billion, the worldwide convertible securities market is larger than most individual investors realize.

TCGCT presents you with another opportunity to attain diversified global exposure and participate in equity returns around the world.

"FAST BREAK" AWARD - Put the world in the palm of your hands! The first 50 Account Executives to post \$20,000 in TCGCT sales will receive a regulation size "Global" Basketball. Dazzle your hoops opponents and dunk the world!!

Speaking of the world...how about a Fall getaway to Bermuda?

GRAND PRIZE DRAWING
Scoop off to Bermuda for a three day/two night Getaway Weekend Vacation. This weekend includes surface, accommodations, hotel taxes, airport transfers and more! All AE's who reach the \$50,000 sales level qualify for a chance to win - every \$10,000 in sales above that level gives you another ticket for the drawing.

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Plymouth Neon

Get up to **\$1,200* OFF**



Chrysler Concorde

Up to **\$1,684** OFF**

Chrysler New Yorker

Get over **\$1,800† OFF**



See Your Local Chrysler-Plymouth Dealer Now.

new '95 stock. Up to \$600 cash back on select option packages. Up to \$600 pkg. values. **\$1,350 cash back on Concorde with D pkg. & 3.5 liter engine plus \$334 in pkg. values. \$1,338 cash back on select option pkgs. and up to \$523 in pkg. values. Pkg. values based on total value of pkg. items vs. usual discounted pkg. MSRP. Always wear your seat belt.

CLOSED-END FUNDS: BRUISED BUT BECKONING

Many have been bashed down to bargain prices, and careful pickers can score

The market has no mercy. If the past year was rough on mutual funds, consider the plight of the closed-end funds. Not only did their portfolios buckle under the weight of rising interest rates but investors dumped them by the bushel. Closed-end fund investors have to sell their shares on the open market instead of requesting the fund company to redeem them. And as they sold out, share prices dropped much farther than the underlying value of their investments: Equity funds saw their portfolio returns drop by 4.6%, while share prices fell 12.5%. Bond funds, with a 3.9% loss in portfolio return, took an even bigger hit—14.9%.

The good news about the 1994 pasting is that closed-end funds are now more attractive than they have been in years. That bargain-counter pricing even extends to some of the funds that earned three upward-pointing arrows—the highest rating for risk-adjusted returns in the BUSINESS WEEK Closed-End Scoreboard.

PITFALLS. Because there are so many more opportunities, we have expanded the Scoreboard to cover 260 closed-end funds, 35 more than last year. The Scoreboard, which is prepared for BUSINESS WEEK by Morningstar Inc., reports one- and three-year returns, by both the change in net asset value (NAV) and by share-price performance in the market. Ratings calculations are based on three-year NAV returns. In most cases, investors will want to buy funds at discount to NAV. That's why the Scoreboard reports how much

higher or lower a fund is trading compared with its NAV.

Start your fund-hunting with those selling at a discount. But watch out. The funds with the largest discounts aren't necessarily the best buys. "You still have to apply all the scrutiny that you would for a mutual fund," says Catherine Gillis, editor of *Morningstar Closed-End Funds*, a publication that reports on the closed-end universe. "For

NESS WEEK's Mutual Fund Scoreboard (Feb. 6).

Bargain hunters may also salivate at discounts in many single-country, emerging-markets funds. Back in 1991, international funds had phenomenal turns—an average 52% NAV gain and 72% in share-price gains. But be wary of jumping in too quickly. "These funds are attractive, but they're not at giveaway prices yet," warns Thomas J. Herz

the dean of closed-end fund investing.

SHORT STORM? So are way overpriced after the bloodletting. Just look at the Mexican Emerging Mexico, Mexico Equity & come funds. Even after a 35% collapse in peso and a 12% fall in stocks, the funds sell at prices significantly higher than their net asset values. A lot of investors, it seems, are trying to ride out what they think is a short-term storm. But if damage turns out to be more long-lasting, then share prices will fall those much diminished NAVs downward. If you're looking for tom-fish for stocks of the border, Herz suggests sticking more diversified regional funds such as the Latin America Equity Fund.

But even buying a fund at an attractive discount does an investor no good if the underlying market is in a funk. "The premium/discount issue is overdone," warns Rory S. Costello, closed-end fund analyst for Prudential Securities. "It's more important to be right on the market." One of Costello's top picks is First Australia Fund, which sells at a 10.8% discount to NAV. "People are leeching on commodities, and this fund

THE BEST CLOSED-END FUNDS

Of the 260 closed-end funds in the Mutual Fund Scoreboard, only these 16 earned three upward-pointing arrows, the highest rating for risk-adjusted total return for the 1992-94 period.

Equity Funds

	AVERAGE ANNUAL TOTAL RETURN*	RISK	INVESTMENT CATEGORY
BRAZIL	38.2%	High	Latin America
FIRST FINANCIAL	41.7	Low	U.S.
FIRST PHILIPPINE	37.3	Average	Pacific
SOUTHEASTERN THRIFT & BANK	35.1	Low	U.S.
THAI	32.0	High	Pacific
THAI CAPITAL	34.3	High	Pacific

Bond Funds

CIGNA HIGH-INCOME	13.2%	Very low	Corp.-high-yield
CIM HIGH-YIELD SECURITIES	12.8	Low	Corp.-high-yield
FRANKLIN UNIVERSAL	11.9	Average	Multisector
KEMPER STRATEGIC MUNI. INCOME	7.2	Low	Municipal
MFS MUNICIPAL INCOME	6.6	Very low	Municipal
NEW AMERICA HIGH INCOME	17.7	Average	Corp.-high-yield
NUVEEN NY MUNI. VALUE	5.5	Low	Municipal
PROSPECT STREET HIGH INCOME	13.7	Low	Corp.-high-yield
PUTNAM HIGH INCOME CONVERTIBLE	15.2	Very Low	Convertible
USF&G PACHOLDER	12.7	Very low	Corp.-high-yield

*1992-94, pretax return based on appreciation of net asset value plus reinvestment of dividends and capital gains

DATA: MORNINGSTAR INC.

instance," she notes, "is the fund well managed?"

A case in point is Engex. This closed-end equity fund invests in emerging growth companies and sells at a 29.3% discount to NAV—the largest discount in the Scoreboard. But that fund is no bargain. Engex' portfolio management has produced a three-year average annual return of -6.6%. That's worse than all but one equity mutual fund in BUSI-

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Performance and rankings are historical and do not represent future results. Yields vary.

^{*}Source: *Money Fund Report*.[®] The Fund's advisor is waiving all management fees and expenses through June 1, 1995. Without this waiver, the current and effective yields would have been 5.28% and 5.47%, respectively. Effective yield assumes reinvestment of dividends. For more complete information, including management fees and expenses, call Strong Funds Distributors, Inc. for a free prospectus kit. Please read it carefully before you invest or send money. 779K94I

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some heavy bets on commodity producers," he says. Costello also recommends the relatively staid New Germany Swiss Helvetia funds rather than betting on a rebound in the volatile T. World funds.

Opportunities abound among the bond funds as well. Herzfeld, in particular, thinks there's good value among "term trusts," the closed-end funds that liquidate within several years. Many of these trusts invested in mortgage derivatives to generate high yields, but their prices collapsed in last year's bond market. "Many will not make their objective of redeeming at \$10 a share," says Herzfeld. "But the term trusts are cheap and the discounts large, so they can still make money."

After the worst bond market in decades, term trusts are a little less risky for most gun-shy analysts to recommend. They're generally advising investors to stick with funds that invest in short to intermediate maturities and have good credit quality. They also want

Gun-shy analysts favor bond funds that are short to intermediate maturities

against funds with exotic mortgage-backed securities and leverage. Many closed-end bond funds borrow on margin or issue preferred stocks to buy more bonds than their asset size would otherwise permit. Morningstar's Gillis at Allmerica Securities, Pacific American Income Shares, and USLife Income funds all fit the "plain-vanilla" bill—and at discounts to NAV to boot.

On the municipal-bond side, caution is the watchword, too. "The funds with the biggest discounts are those with the best coupon bonds and the longest maturities," warns Mariana F. Bush, an analyst for Kemper Securities Inc. "The funds may not be right for conservative investors who buy funds for income."

However, if you want to make a bet on falling interest rates, funds with higher yields and the longest maturities are the ideal maneuver. If rates do fall, the NAVs will rise and their discounts narrow—and investors will make a comfortable score. You can find these funds—well as the more cautious sorts—in the Scoreboard that starts next page.

*By Jeffrey M. Laderman
in New York*

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MUTUAL FUND SCOREBOARD

Closed-End Equity Funds

	RATING	CATEGORY	RISK	SIZE ASSETS \$MIL	FEES EXPENSE RATIO (%)	1994 RESULTS				YIELD (%)	TREND 3-YEAR ANALYSIS	PREMIUM/DISCOUNT	
						NAV RET (%)		SHARES RET (%)				DIFFERENCE FROM NAV	
						1 YR.	3 YRS	1 YR.	3 YRS			1994 HIGH-LOW	2/3/95
MS EXPRESS	AVG	U. S.	Low	798.3	0.32	0.1	5.9	-3.8	3.2	3.0		-7.6-14.5	-13.5
ANCE GLOBAL ENVIRONMENT	◆◆◆	World	Average	76.6	1.67	-2.1	-6.2	-9.1	-9.0	0.0		-10.2-22.2	-21.4
ERICA'S ALL SEASON	◆◆◆	World	Low	41.1	2.54	-7.7	-2.6	-15.0	-2.7	3.1		-14.8-28.7	-27.2
ENTINA FUND	◆	Latin America	High	108.1	1.87	-15.2	4.5	-25.0	-2.7	2.2		16.0-7.3	8.1
LIMITED	AVG	World	Very high	503.1	0.41	2.1	12.8	-4.8	3.3	3.1		5.8-19.3	1.9*
A PACIFIC	◆◆	Pacific	High	206.1	2.06	-21.7	22.3	-35.3	20.6	0.1		27.7-6.3	3.6
TIGERS	◆◆	Pacific	High	243.6	1.60	-18.4	NA	-41.5	NA	0.4		17.0-21.1	-11.1
TRIA FUND	◆◆	Europe	High	107.9	1.87	-4.2	1.0	-15.4	-1.2	0.3		6.7-17.6	-12.3
ER FENTRESS	AVG	U. S.	Low	461.9	0.86	-3.6	5.0	-7.5	3.6	2.3		-13.4-21.4	-18.3
GSTROM CAPITAL	◆◆	U. S.	Average	114.7	0.41	6.4	1.0	-3.9	-7.0	1.4		2.2-11.4	-12.7
E CHIP VALUE	AVG	U. S.	Low	76.5	1.19	0.8	4.8	-13.2	3.5	1.6		6.3-14.3	-13.3
ZIL FUND	◆◆◆	Latin America	High	376.4	1.74	61.0	38.2	69.7	37.9	0.0		12.7-13.3	1.0*
ZILIAN EQUITY	◆◆	Latin America	High	91.4	1.85	48.8	NA	53.4	NA	0.1		30.6-10.5	8.7*
TRAL FUND OF CANADA	◆	U. S.	Average	85.5	0.81	-4.5	3.5	-8.4	6.8	0.0		14.1-1.4	-3.5*
TRAL SECURITIES	◆◆	U. S.	Low	226.6	0.57	8.7	24.5	12.3	31.4	1.3		-2.3-12.2	-6.2*
RLES ALLMON TRUST	AVG	U. S.	Very low	112.8	1.45	0.6	3.7	-11.6	-0.3	2.6		-1.6-14.6	-15.7
E FUND	◆◆	Latin America	Average	367.1	1.48	33.5	30.2	6.1	34.1	2.0		13.1-18.4	-11.2
IA FUND	◆◆	Pacific	High	136.3	2.50	-31.2	NA	-48.9	NA	0.1		30.0-1.4	12.6
MENTE GLOBAL GROWTH	AVG	World	Low	63.2	1.95	-3.0	9.7	-15.9	7.3	0.0		-5.8-22.8	-18.6*
EN & STEERS REALTY INCOME	◆	Income	Low	23.5	1.38	3.5	13.0	-2.9	15.1	7.9		12.7-0.1	8.5
EN & STEERS TOTAL RETURN	◆◆	U. S.	High	101.4	1.13	6.3	NA	-2.3	NA	7.1		8.3-6.7	5.0
NSELLORS TANDEM	◆◆◆	U. S.	High	69.3	1.35	-16.8	-4.2	-12.0	-1.9	0.0		-8.9-19.9	-12.0
AWARE GROUP DIV. & INCOME	◆◆	Income	Average	221.5	1.00	-5.4	NA	-12.2	NA	9.5		7.1-10.9	-3.5
F & PHELPS UTILITIES INCOME	◆◆	Income	Average	2010.0	1.14	-15.9	0.1	-14.5	1.9	9.1		14.7-2.2	11.7
RGING GERMANY	◆◆	Europe	Average	130.6	1.40	-4.9	1.8	-21.3	-0.7	0.0		-5.6-20.9	-19.5
RGING MARKETS INFRASTRUCT.	◆◆	World	High	209.7	1.99	-6.0	NA	-35.7	NA	0.2		11.7-21.3	-16.9
RGING MARKETS TELECOM.	◆◆	World	High	161.1	1.81	-3.5	NA	-29.0	NA	0.9		19.0-10.2	-2.7
RGING MEXICO	◆◆	Latin America	Very high	90.5	1.56	-39.8	2.9	-33.6	12.2	1.8		26.4-9.0	32.1*
EX	◆◆◆	U. S.	Very high	11.7	2.99	-32.9	-6.6	-35.3	-7.7	0.0		-12.3-31.7	-29.3
PE FUND	AVG	Europe	Average	126.2	1.48	7.3	8.1	-9.9	6.0	8.9		1.9-16.3	-8.5
PEAN WARRANT	◆◆	Europe	Very high	67.2	1.66	-32.8	21.0	-41.2	18.3	0.0		10.9-17.9	-16.0*
T AUSTRALIA	◆◆	Pacific	High	163.4	1.45	-2.5	5.5	-14.6	5.0	1.5		2.5-19.1	-10.8
T FINANCIAL	◆◆◆	U. S.	Low	172.2	1.51	13.8	41.7	12.5	42.2	0.3		4.4-12.3	1.5
T IBERIAN	◆◆	Europe	High	57.0	2.19	-0.2	0.7	-16.2	-0.6	0.0		5.6-19.9	-18.1
T ISRAEL	◆◆	World	High	53.7	2.64	-33.8	NA	-35.2	NA	0.0		26.4-5.6	-1.4
T PHILIPPINE	◆◆◆	Pacific	Average	212.0	1.79	2.7	37.3	-6.7	40.5	0.0		-10.4-25.8	-24.3
ICE GROWTH	◆	Europe	Average	168.4	1.64	-5.8	4.4	-25.6	4.7	0.3		8.3-17.8	-13.4
IRE GERMANY	AVG	Europe	Average	219.0	1.19	6.2	9.5	-9.6	5.6	1.4		-6.7-21.7	-18.7
ELLI EQUITY	◆	U. S.	Low	823.1	1.17	0.6	12.1	-5.2	15.1	1.2		12.3-0.3	1.0
NI II CAPITAL	AVG	U. S.	Average	207.8	0.00	-8.1	10.4	-8.3	14.1	0.0		-9.2-17.9	-12.5
NI II INCOME	◆◆	Income	Very low	102.0	NA	16.8	14.9	4.2	6.0	16.5		26.3-5.2	17.7
TRAL AMERICAN INVESTORS	◆◆	U. S.	Average	519.7	1.13	-2.8	-0.3	-7.9	-3.8	0.3		-8.6-15.3	-15.5
ANY FUND	AVG	Europe	Average	173.9	1.36	8.4	10.4	-7.4	0.8	1.8		2.0-16.9	-12.5
IAL HEALTH SCIENCES	◆	U. S.	High	255.5	1.41	2.2	NA	-9.2	NA	0.0		-9.8-20.9	-18.7
IAL SMALL CAP	◆	World	High	47.3	1.79	-17.3	NA	-32.0	NA	0.0		1.7-20.7	-17.6
TER CHINA	◆	Pacific	High	137.0	2.09	-36.5	NA	-52.1	NA	0.8		18.9-15.2	0.0
TH FUND OF SPAIN	◆◆	Europe	High	196.3	1.23	3.2	0.6	-2.9	2.0	4.7		-5.2-20.2	-18.6
GLOBAL DEVELOPING MKTS. \$	◆	World	High	452.9	2.03	NA	NA	NA	NA	NA		1.9-22.6	-16.4
GREATER EUROPE	AVG	Europe	Average	226.2	1.82	-0.5	9.1	-16.1	9.2	0.2		0.8-16.9	-11.0
HEALTHCARE INVESTORS	◆◆◆	U. S.	Very high	87.3	1.74	-12.6	-8.0	-18.2	-15.4	0.0		2.8-15.9	-10.9

2/2/95. ** As of 2/1/95. NA = Not available. \$ = New fund; less than 12 months' total return.

DATA: MORNINGSTAR INC., CHICAGO, IL.

To Use the Tables

Closed-end funds are publicly traded investment companies. Results are measured two ways, by the change in net asset value (NAV), which is generated by the fund's manager; the other by the change in the market price. Total returns, which include dividends and capital gains, are shown for three-year periods. The star figure is an average annual return. All returns are pretax.

STARS WEEK RATING

are based on three-year adjusted performance of the portfolio. A rating is calcu-

lated by subtracting a fund's risk-of-loss factor from total return. Equity funds are rated against each other, and to earn an above-average rating, must beat the S&P 500 on a risk-adjusted basis. For ratings, municipal bond funds are separated from other bond funds.

- ◆◆◆ SUPERIOR
- ◆◆ VERY GOOD
- ◆ GOOD
- AVG AVERAGE
- ◆ BELOW AVERAGE
- ◆ POOR
- ◆◆ VERY POOR

RISK

For each fund, the monthly Treasury bill return is subtracted from the monthly NAV return in each

month of the rating period. When a fund has underperformed Treasury bills, this monthly result is negative. The sum of these negative numbers is then divided by the number of months. The result is a negative number, and the greater its magnitude, the higher the risk of loss.

EXPENSE RATIO

Fund expenses for 1994 as a percentage of average net assets. Ratio may include interest expense.

YIELD

Income earned during 1994, as a percentage of yearend NAV per share, adjusted for capital gains.

MATURITY

The average maturity of the secu-

rities in a bond fund, weighted according to their market value.

TREND

A fund's relative performance during 1992, 1993, and 1994. From left to right, the level of green in each shows how the portfolio of each fund performed relative to other funds: ■ for the top quartile; ■ for the second quartile; ■ for the third quartile; and ■ for the bottom quartile. An empty box indicates no returns for that time period.

PREMIUM/DISCOUNT

The market price of closed-end funds is either less than the value of their securities, a discount, or more, a premium, to their NAVs.

MUTUAL FUND SCOREBOARD

Closed-End Equity Fund

	RATING	CATEGORY	RISK	SIZE ASSETS \$MIL	FEES EXPENSE RATIO (%)	1994 RESULTS					TREND 3-YEAR ANALYSIS	PREMIUM/DISCOUNT	
						NAV RET (%)		SHARES RET (%)		YIELD (%)		DIFFERENCE FROM NAV	
						1 YR.	3 YRS.	1 YR.	3 YRS.			1994 HIGH-LOW	2/3/95
H&Q LIFE SCIENCES INVESTORS		U. S.		69.2	1.87	-23.0	NA	-26.5	NA	0.0		-0.5 -20.0	-10.8
INDIA FUND \$		Pacific		473.1	2.01	NA	NA	NA	NA	NA		9.5 -24.6	-19.3
INDIA GROWTH	▲	Pacific	Very high	146.8	2.22	23.3	16.7	-21.3	24.0	0.0		54.3 -9.7	1.7
INDONESIA FUND	▼	Pacific	High	42.3	1.61	-34.6	5.9	-42.2	12.7	0.0		41.5 -13.5	29.9
INEFFICIENT MARKET	AVG	U. S.	Average	51.6	1.22	-4.4	5.2	-8.2	3.0	0.5		-14.2 -22.1	-20.5
IRISH INVESTMENT	▼	Europe	Average	51.4	1.87	5.4	3.5	-5.6	5.9	0.0		-2.4 -16.0	-15.1
ITALY FUND	▼▼	Europe	Very high	89.4	1.70	-0.1	-2.9	-19.1	0.6	2.1		15.2 -17.4	-14.4
JAKARTA GROWTH	▲	Pacific	High	43.2	1.84	-15.1	12.4	-34.3	16.9	0.3		24.9 -1.2	8.8
JAPAN EQUITY		Pacific		102.8	0.93	39.3	NA	13.3	NA	0.0		28.6 -6.0	2.2
JAPAN OTC EQUITY	▼▼	Pacific	Very high	115.4	1.39	13.2	0.0	-1.3	-2.1	0.0		33.3 -9.3	5.0
JARDINE FLEMING CHINA		Pacific		114.5	1.93	-40.0	NA	-52.1	NA	0.2		31.7 -10.6	-1.5
JOHN HANCOCK PATRIOT GLOBAL (a)		Income		156.8	1.27	-11.2	NA	-26.3	NA	12.4		9.9 -13.8	-4.4
JOHN HANCOCK PAT. PREFERRED (b)		Income		134.5	1.24	-8.8	NA	-15.4	NA	11.1		5.4 -11.7	-2.0
JOHN HANCOCK PAT. PREMIUM I (c)	▼	Income	Average	183.7	1.29	-14.7	2.2	-14.3	3.4	10.7		9.4 -4.3	3.7
JOHN HANCOCK PAT. PREMIUM II (d)	▼	Income	Average	244.3	1.25	-16.6	1.9	-16.3	1.2	10.1		-0.9 -9.1	-1.5
JOHN HANCOCK PATRIOT SELECT (e)	▼	Income	Average	195.8	1.30	-14.2	1.3	-14.2	-2.1	10.6		2.6 -8.9	0.6
JUNDT GROWTH	▼	U. S.	Average	223.3	1.55	4.8	1.8	4.3	-2.2	0.0		-2.3 -10.5	-7.5
KOREA FUND	▲	Pacific	High	610.0	1.37	24.8	26.2	-4.7	22.8	0.0		37.0 -2.7	8.2
KOREA EQUITY		Pacific		82.5	1.52	-9.3	NA	-37.3	NA	0.0		28.5 -15.7	-9.6
KOREAN INVESTMENT		Pacific		87.4	2.26	18.8	NA	-27.2	NA	0.0		34.0 -16.5	4.9
LATIN AMERICA EQUITY	▲	Latin America	High	154.8	1.81	3.1	21.3	-11.0	25.4	0.8		19.9 -18.0	-4.4
LATIN AMERICA INVESTMENT	▲	Latin America	High	156.6	1.81	3.4	19.3	-21.7	17.4	0.3		18.8 -16.5	-1.2
LATIN AMERICAN DISCOVERY		Latin America		135.3	2.12	0.8	NA	-7.9	NA	0.0		14.1 -13.5	1.2
LIBERTY ALL-STAR EQUITY	AVG	U. S.	Low	698.0	1.08	-1.3	4.7	-16.7	2.7	5.4		8.4 -9.7	-6.3
MALAYSIA FUND	▲	Pacific	High	180.9	1.29	-23.7	23.9	-30.5	27.0	0.0		17.4 -9.7	-1.2
MEXICO FUND	▼	Latin America	Very high	765.4	0.92	-43.3	4.4	-41.4	12.6	1.0		14.5 -10.5	17.8
MEXICO EQUITY & INCOME	▼	Latin America	High	103.0	1.64	-27.7	8.0	-20.6	23.4	0.0		26.7 -10.7	29.9
MFS SPECIAL VALUE	▲	U. S.	Low	72.6	1.20	-7.5	9.1	-7.2	13.1	0.5		22.6 -4.4	13.0
MORGAN GRENFELL SMALLCAP	▼	U. S.	Average	59.1	1.46	-1.9	3.8	-6.6	-2.3	0.0		-2.7 -18.4	-13.3
MORGAN STANLEY AFRICA INV. \$		World		222.0	2.16	NA	NA	NA	NA	NA		12.0 -23.3	-16.5
MORGAN STANLEY EMERG. MKTS.	▲	World	Average	317.3	1.74	-6.8	27.9	-10.8	31.6	0.0		15.9 -6.0	6.4
MORGAN STANLEY INDIA INVEST. \$		Pacific		499.5	1.40	NA	NA	NA	NA	NA		6.6 -19.6	-16.6
NAIC GROWTH	AVG	U. S.	Low	8.3	1.64	3.2	5.7	0.9	1.1	0.9		4.1 -21.0	-17.1
NEW AGE MEDIA		U. S.		201.0	1.35	-0.9	NA	-19.6	NA	0.1		9.1 -20.0	-15.3
NEW GERMANY	AVG	Europe	Average	472.6	1.06	3.9	6.3	-12.5	3.7	1.4		-8.7 -21.5	-18.2
PAKISTAN INVESTMENT		Pacific		132.3	2.16	-18.5	NA	-41.8	NA	0.3		11.3 -24.5	-20.8
PETROLEUM & RESOURCES	AVG	U. S.	Low	332.3	0.50	-2.1	6.3	-0.7	6.9	3.5		-1.1 -6.0	-3.9
PILGRIM REGIONAL BANKSHARES	▲	U. S.	Low	151.7	1.48	-1.9	12.3	-8.9	8.6	1.9		-3.8 -15.6	-11.7
PORTUGAL FUND	AVG	Europe	High	75.9	1.35	11.2	10.4	-1.4	12.9	0.4		9.5 -13.0	-6.5
PREFERRED INCOME	▲	Income	Very low	189.0	1.52	-4.4	11.0	-9.8	4.0	10.7		3.0 -14.2	0.6
PREFERRED INCOME MGMT.		Income		192.3	1.81	-4.9	NA	-10.2	NA	10.4		0.4 -15.0	-3.7
PREFERRED INCOME OPPORTUNITY		Income		187.2	1.69	-4.7	NA	-14.9	NA	11.5		1.6 -14.1	-1.2
PUTNAM DIVIDEND INCOME	AVG	Income	Very low	107.4	1.42	-7.5	7.1	-9.4	3.7	9.1		-5.7 -15.7	-11.0
QUEST FOR VALUE CAPITAL	▲	U. S.	Low	464.4	0.00	-0.8	11.6	-0.1	16.6	0.0		-9.9 -17.7	-11.6
QUEST FOR VALUE INCOME	▲	Income	Very low	209.3	0.74	11.4	10.9	1.8	7.3	11.0		15.1 -2.2	4.0
R. O.C. TAIWAN	▲	Pacific	Average	365.7	1.98	23.5	11.8	-13.6	5.5	0.0		21.6 -13.8	-3.1
ROYCE OTC MICRO-CAP		U. S.		82.5	1.70	5.0	NA	-6.0	NA	0.3		6.2 -12.9	10.4
ROYCE VALUE	▲	U. S.	Very low	309.0	1.52	0.6	12.2	-6.2	10.8	0.1		-3.7 -15.4	-8.0
SALOMON BROS.	AVG	U. S.	Low	1086.7	0.48	-0.1	5.9	-5.4	2.8	2.8		-9.7 -18.4	-15.7
SCHRODER ASIAN GROWTH		Pacific		251.7	1.59	-8.4	NA	-34.9	NA	0.0		14.5 -20.8	-11.2
SCUDDER NEW ASIA	▲	Pacific	Average	182.4	1.67	-12.0	15.9	-24.2	13.1	1.0		10.8 -11.5	4.9
SCUDDER NEW EUROPE	▼	Europe	Average	177.4	1.67	-0.3	4.2	-15.1	3.5	0.0		3.1 -18.2	-17.3
SINGAPORE FUND	▲	Pacific	High	97.4	1.90	-4.7	16.3	-26.4	26.2	0.0		26.3 -9.4	12.1
SOURCE CAPITAL	AVG	U. S.	Very low	329.4	1.01	0.7	6.6	-6.1	2.9	3.7		10.5 -3.9	-1.1
SOUTHEASTERN THRIFT & BANK	▲	U. S.	Low	39.5	1.46	7.6	35.1	11.1	43.7	1.3		4.7 -13.0	-5.1
SPAIN FUND	▼	Europe	High	94.2	2.00	-2.5	-5.7	-26.1	-12.6	0.0		16.0 -13.5	-13.0
SWISS HELVETIA	▼	Europe	Low	181.8	1.48	1.1	16.4	-11.2	16.3	1.4		6.4 -8.6	-7.5
TAIWAN FUND (f)	▲	Pacific	Average	289.5	2.49	22.9	15.4	-26.2	5.9	0.1		32.1 -13.9	2.4
TEMPLETON CHINA WORLD		Pacific		230.0	1.84	-31.8	NA	-44.6	NA	1.8		14.5 -11.4	0.3
TEMPLETON EMERGING MKTS.	▲	World	Average	288.9	1.78	-11.5	21.5	-20.2	14.2	0.4		31.0 -0.6	19.1
TEMPLETON GLOBAL UTILITIES	▲	World	Low	40.3	1.21	-6.1	9.7	-12.7	12.1	3.9		13.0 -9.0	-3.1
THAI FUND	▲	Pacific	High	343.8	1.33	-13.7	32.0	-27.0	20.3	1.3		4.1 -21.8	-14.2
THAI CAPITAL	▲	Pacific	High	124.8	2.29	-12.2	34.3	-24.4	25.6	0.0		4.6 -19.1	-10.1
TRI-CONTINENTAL	AVG	U. S.	Low	2031.7	0.65	-2.2	4.6	-4.5	-0.4	3.6		-11.7 -16.9	-15.1
TURKISH INVESTMENT	▼	Europe	Very high	33.5	2.16	-58.3	-14.3	-59.8	-9.1	2.1		100.3 -9.0	21.1
UNITED KINGDOM FUND	AVG	Europe	Average	51.2	1.51	4.0	10.5	-15.2	10.0	4.0		0.1 -18.1	-14.1
WORLDWIDE VALUE	▼	World	Average	53.4	2.00	-3.7	5.1	-14.3	4.8	0.0		-4.0 -21.0	-19.1
Z SEVEN	▼	World	Average	25.8	3.22	-1.9	-1.1	-9.6	-7.7	0.0		8.8 -3.5	1.1
ZIG	▼	U. S.	Low	492.0	1.23	-2.7	3.5	-16.2	0.1	0.4		19.9 -0.7	7.7
ZWING TOTAL RETURN	AVG	U. S.	Very low	591.7	1.10	-1.0	3.6	-17.3	-0.1	4.3		18.4 -1.4	4.1

* As of 2/2/95. ** As of 2/1/95. NA = Not available. \$ New fund; less than 12 months' total return. (a) Formerly Patriot Global Dividend. (b) Formerly Patriot Preferred Dividend. (c) Formerly Patriot Premium Dividend I. (d) Formerly Patriot Premium Dividend II. (e) Formerly Patriot Select Dividend. (f) To calculate NAV return and premium/discount, Morningstar adds the \$6.09 yearend distribution to the fund's NAV.

DATA: MORNINGSTAR INC., CHICAGO

-609-786-4415

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MUTUAL FUND SCOREBOARD

Closed-End Bond Funds

	RATING	CATEGORY	RISK	SIZE	FEES	1994 RESULTS				PORTFOLIO		TREND	PREMIUM/DISCOUNT	
						ASSETS \$MIL	EXPENSE RATIO (%)	NAV RET (%)		SHARES RET (%)			YIELD (%)	MAT (YRS.)
						1 YR	3 YRS	1 YR	3 YRS				1994 HIGH-LOW	2/3
ACM GOVERNMENT INCOME	☆☆	Multisector	Very high	528.5	1.52	-14.7	4.4	-17.8	5.4	11.0	9.2		22.4-1.2	13.1
ACM GOVERNMENT OPPORTUNITY	☆☆	Multisector	High	97.2	1.20	-13.0	4.1	-15.1	4.8	10.6	12.1		6.8-11.2	-2.1
ACM GOVERNMENT SECURITIES	☆☆	Multisector	Very high	692.8	1.41	-15.8	3.7	-23.7	3.4	12.4	13.3		12.8-6.3	7.1
ACM GOVERNMENT SPECTRUM	☆☆	Multisector	Very high	256.9	1.18	-18.2	2.8	-20.5	4.4	12.4	14.5		15.1-7.8	7.1
ACM MANAGED INCOME	☆☆	Multisector	High	247.3	1.14	-12.4	10.3	-18.0	13.7	12.0	10.7		22.1-0.5	5.1
ACM MANAGED MULTI MKT. TRUST	☆☆☆☆	International	High	80.4	1.23	-10.6	-1.8	-7.8	-8.0	9.4	2.3		1.6-12.6	5.1
AIM STRATEGIC INCOME	AVG	Convertible	Very low	64.0	1.54	0.3	7.3	-5.3	5.1	5.6	9.6		-6.8-15.2	12.1
ALLAMERICA SECURITIES TRUST (g)	AVG	Corp General	Average	91.4	0.77	-2.0	7.0	-12.6	4.0	9.1	9.4		-2.6-18.7	-8.1
AMERICAN ADJ. RATE TERM 1995	AVG	Government	Low	104.8	0.77	1.9	4.2	-2.1	1.7	3.1	1.5		3.6-5.1	-2.1
AMERICAN ADJ. RATE TERM 1996	☆☆	Government	Low	218.4	0.65	-3.6	2.8	-8.1	-1.5	5.0	5.0		2.7-8.9	-7.1
AMERICAN ADJ. RATE TERM 1997	☆☆	Government	Low	456.1	0.61	-5.2	2.6	-10.1	-2.1	6.2	5.4		1.8-11.6	-10.1
AMERICAN CAPITAL BOND	☆☆	Corp General	High	231.3	0.68	-7.3	5.2	-12.2	1.2	9.2	19.0		-2.8-13.7	-7.1
AMERICAN CAPITAL CONV. SECS.	AVG	Convertible	Average	70.1	0.87	-5.5	6.9	-11.9	5.7	6.0	11.5		-7.4-16.7	-9.1
AMERICAN CAPITAL INCOME	☆☆	Corp General	Low	111.3	0.99	-2.3	8.3	-8.1	5.8	10.2	14.1		-0.7-13.7	-2.1
AMERICAN GOVT. INCOME	☆☆☆☆	Government	Very high	126.3	1.32	-26.0	-1.5	-24.5	2.2	13.6	11.9		23.3-3.6	13.1
AMERICAN GOVT. INCOME PORT.	☆☆☆☆	Government	Very high	178.1	1.28	-25.9	-1.3	-24.8	1.9	14.6	11.6		23.6-2.8	14.1
AMERICAN GOVT. TERM TRUST	☆☆☆☆	Government	High	66.9	0.81	-13.9	-0.3	-12.5	-0.6	7.9	10.0		14.2-1.3	-7.1
AMERICAN MUNICIPAL TERM TRUST	AVG	Municipal	Average	131.4	0.59	-5.7	8.2	-2.0	5.9	6.5	13.2		-2.0-10.0	-7.1
AMERICAN MUNICIPAL TERM TRUST II	AVG	Municipal	High	112.6	0.64	-6.3	8.2	-4.7	5.3	6.5	14.3		-3.1-11.0	-6.1
AMERICAN OPPORTUNITY INCOME	☆☆☆☆	Government	Very high	162.3	1.39	-27.9	-2.5	-24.2	1.9	14.7	12.5		32.9-8.8	25.1
APEX MUNICIPAL	☆☆	Municipal	Low	188.5	0.88	-0.7	4.4	-6.9	-1.7	8.5	21.9		1.9-16.7	-7.1
BANCROFT CONVERTIBLE	☆☆	Convertible	Low	62.0	1.20	-2.4	10.2	-10.6	10.8	6.1	11.2		0.7-14.0	-11.1
BLACKROCK ADVANTAGE TERM TR.	☆☆	Government	High	135.6	1.05	-8.6	1.6	-21.6	-4.2	9.4	10.0		0.6-17.3	-14.1
BLACKROCK INCOME	☆☆	Government	High	569.1	1.06	-6.7	-0.5	-14.7	-8.1	12.5	9.0		1.0-17.4	-8.1
BLACKROCK MUNICIPAL TARGET	☆☆	Municipal	High	678.4	0.90	-5.9	7.9	-8.9	3.5	6.9	12.0		-2.9-12.7	-6.1
BLACKROCK 1998 TERM TRUST	☆☆	Government	High	647.9	0.85	-2.9	2.4	-15.1	-1.8	7.9	4.5		2.5-9.5	-5.1
BLACKROCK NORTH AMER. GOVT.	☆☆	International	Very high	539.2	1.02	-13.4	-3.4	-17.9	-9.1	12.5	12.1		4.4-15.4	-5.1
BLACKROCK STRATEGIC TERM	☆☆	Government	High	647.7	0.98	-6.1	0.9	-20.8	-4.9	8.8	9.5		3.4-18.1	-13.1
BLACKROCK TARGET TERM TRUST	☆☆	Government	High	1169.4	0.74	-6.2	2.6	-12.0	-2.0	8.8	6.5		-1.0-11.2	-7.1
CASTLE CONVERTIBLE	☆☆	Convertible	Very low	54.1	1.05	-1.3	10.2	-2.0	14.4	6.5	11.7		0.9-13.4	-4.1
CIGNA HIGH-INCOME	☆☆	Corp Hi Yld	Very low	324.2	3.11	-1.6	13.2	-5.6	12.2	12.9	8.3		18.9-2.2	1.1
CIM HIGH-YIELD SECURITIES	☆☆	Corp Hi Yld	Low	51.2	2.06	-0.9	12.8	1.0	16.3	11.8	6.2		7.4-4.1	1.1
CIRCLE INCOME SHARES	AVG	Corp General	Average	30.9	0.89	-3.2	5.4	-10.8	-0.2	9.2	8.6		2.5-12.9	-11.1
CNA INCOME SHARES	AVG	Corp General	Average	103.2	0.96	-4.9	5.6	-17.6	4.8	11.7	12.4		20.5-3.1	3.1
COLONIAL HIGH-INCOME MUNICIPAL	☆☆	Municipal	Low	246.1	1.01	-0.8	4.1	-9.8	0.3	8.9	23.9		-1.0-16.6	-3.1
COLONIAL INTERMARKET INCOME	☆☆	Multisector	Average	114.4	0.98	-3.7	7.6	-10.7	7.2	10.0	9.8		5.3-13.8	0.1
COLONIAL INTERMED. HIGH-INCOME	☆☆	Corp Hi Yld	Very low	113.0	2.78	-1.1	11.7	1.3	14.2	11.1	7.7		7.5-8.3	3.1
COLONIAL INV. GRADE MUNICIPAL	☆☆	Municipal	Average	114.3	0.86	-4.0	3.2	-8.1	-1.2	7.3	22.4		4.2-11.2	-4.1
COLONIAL MUNICIPAL INCOME	☆☆	Municipal	Very low	195.6	0.83	-0.1	4.2	-13.5	2.1	9.3	22.1		9.4-14.9	-0.1
CONVERTIBLE HOLDINGS CAPITAL	☆☆	Convertible	High	129.9	0.00	-15.6	4.7	-17.2	13.8	0.0	6.2		-15.9-28.1	-13.1
CS FIRST BOSTON INCOME (h)	☆☆	Corp General	Average	196.4	0.86	-1.0	9.5	-8.8	4.1	11.1	8.7		-6.3-16.8	-6.1
CS FIRST BOSTON STRAT. INC. (i)	☆☆	Multisector	Average	78.3	1.02	-2.1	9.5	-4.0	2.8	10.6	9.9		-7.7-15.9	-9.1
CURRENT INCOME SHARES	AVG	Corp General	High	45.7	0.80	-5.0	6.0	-8.4	1.5	8.6	15.2		-8.0-14.5	-9.1
DEAN WITTER GOVT. INCOME	AVG	Government	Low	466.4	0.70	-0.5	3.7	-7.1	0.9	8.1	8.1		-4.3-15.0	-9.1
DREYFUS MUNICIPAL INCOME	AVG	Municipal	Average	182.2	0.85	-5.4	4.8	-10.1	3.6	7.8	23.1		4.8-11.1	-0.1
DREYFUS STRAT. GOVTS. INCOME	☆☆	Multisector	Average	144.2	0.89	-1.6	4.3	-8.8	-0.1	9.9	10.1		-0.3-14.7	-9.1
DREYFUS STRAT. MUNICIPAL BD.	AVG	Municipal	Average	402.8	0.84	-4.6	4.4	-14.2	2.4	7.9	22.7		6.5-10.2	0.1
DREYFUS STRAT. MUNICIPAL	☆☆	Municipal	Low	526.8	0.86	-1.7	5.4	-9.6	1.8	8.0	21.5		9.3-8.6	2.1
DUFF & PHELPS UTIL. TAX-FREE	☆☆	Municipal	High	183.9	1.31	-7.6	6.2	-14.9	1.1	7.5	15.5		1.9-11.6	-4.1
1838 BOND-DEBENTURE	AVG	Corp General	Average	71.5	0.89	-4.5	6.4	-7.9	4.0	9.1	21.5		3.8-6.9	-0.1
ELLSWORTH CONVERT. GR. & INC.	☆☆	Convertible	Low	59.4	1.10	-2.7	10.0	-8.3	10.4	6.4	10.8		-5.4-15.6	-12.1
EXCELSIOR INCOME SHARES	AVG	Corp General	Average	37.5	0.89	-2.3	5.2	-9.6	1.0	7.0	12.0		-9.1-16.7	-12.1
FIRST AUSTRALIA PRIME INCOME	☆☆	International	Very high	1558.2	1.41	5.3	5.7	-13.2	2.0	11.8	6.8		16.0-12.6	-4.1
FIRST COMMONWEALTH	☆☆	International	Average	142.5	1.79	-2.3	NA	-9.8	NA	10.1	8.0		0.6-20.3	-13.1
FORT DEARBORN INCOME	AVG	Corp General	High	131.6	0.72	-4.8	5.4	-9.8	1.4	8.5	17.6		-5.2-13.6	-10.1
FORTIS SECURITIES	AVG	Corp General	Average	107.5	0.76	-4.9	4.9	-14.5	-1.2	11.0	9.3		9.1-7.9	5.1
FRANKLIN MULTI-INCOME	☆☆	Multisector	High	69.5	3.26	-6.8	9.0	-12.9	6.2	9.7	9.3		-0.6-17.5	-6.1
FRANKLIN PRINCIPAL MATURITY	☆☆	Multisector	Very high	221.5	2.26	-14.9	5.4	-18.8	0.6	9.0	6.7		-8.1-16.5	-11.1
FRANKLIN UNIVERSAL	☆☆	Multisector	Average	301.4	2.30	-5.3	11.9	-5.0	11.0	10.5	9.9		-2.1-15.3	-7.1
GLOBAL GOVERNMENT PLUS	☆☆	International	High	308.8	1.09	-5.4	4.0	-12.0	-0.1	8.0	7.2		-8.2-20.6	-15.1
GLOBAL INCOME PLUS	☆☆	International	Average	224.9	1.11	-3.6	4.5	-5.0	0.6	8.3	11.6		0.6-16.8	-4.1
GLOBAL YIELD	☆☆	International	High	493.8	1.01	-8.7	2.2	-17.8	-1.0	5.5	7.3		-7.5-20.8	-17.1
HATTERAS INCOME SECURITIES	☆☆	Corp General	Low	50.2	0.92	-1.7	7.3	-9.6	3.4	9.7	14.6		10.3-3.5	2.1
HIGH INCOME ADVANTAGE	☆☆	Corp Hi Yld	Low	150.9	0.98	-8.0	10.9	-1.9	16.5	11.9	8.1		10.3-4.2	6.1
HIGH INCOME ADVANTAGE II	☆☆	Corp Hi Yld	Low	202.3	0.94	-7.2	12.7	-4.8	16.4	12.5	8.0		4.2-11.5	4.1
HIGH INCOME ADVANTAGE III	☆☆	Corp Hi Yld	Low	78.2	1.00	-7.5	10.8	-3.1	15.0	11.8	8.0		8.0-4.6	5.1
HIGH YIELD INCOME	☆☆	Corp Hi Yld	Very low	93.6	2.29	-4.3	10.6	-8.7	13.4	12.9	8.5		12.2-0.2	6.1
HIGH YIELD PLUS	☆☆	Corp Hi Yld	Low	104.5	2.76	-5.0	11.3	-9.2	12.1	11.9	8.7		4.7-5.8	0.1
HYPERION TOTAL RETURN	AVG	Multisector	Average	332.7	2.63	0.7	4.9	-11.5	-1.0	12.8	5.5		2.0-20.4	12.1
INA INVESTMENT SECURITIES	AVG	Corp General	Average	84.1	0.94	-2.4	6.2	-8.4	3.3	8.7	11.3		-7.0-14.7	-11.1

* As of 2/2/95. ** As of 2/1/95. NA = Not available. † New fund; less than 12 months' total return. (g) Formerly State Mutual Securities. (h) Formerly First Boston Income. (i) Formerly First Boston Strategic Income.

DATA: MORNINGSTAR INC., CHICAGO

MUTUAL FUND SCOREBOARD

Closed-End Bond Funds

	RATING	CATEGORY	RISK	SIZE ASSETS \$MIL	FEES EXPENSE RATIO (%)	1994 RESULTS				PORTFOLIO		TREND 3-YEAR ANALYSIS	PREMIUM/DISCOUNT	
						NAV RET (%)		SHARES RET (%)		YIELD (%)	MAT (YRS.)		DIFFERENCE FROM NAV	
						1 YR	3 YRS	1 YR	3 YRS				1994 HIGH-LOW	2/3/95
DEPENDENCE SQUARE INCOME	AVG	Corp General	Average	30.4	0.84	-2.8	7.1	-4.4	5.6	8.3	20.4		-2.3 -13.8	-9.7
ERCAPITAL INCOME SECURITIES	AVG	Corp General	Average	204.2	0.68	-2.4	5.9	-11.4	-1.6	10.2	22.5		9.5 -6.7	3.5
ERCAPITAL INSURED MUNI. BD.	◆	Municipal	High	104.4	1.03	-7.2	6.1	-15.2	3.5	7.9	26.5		8.8 -10.4	-4.2
ERCAPITAL QUALITY MUNI. INV.	◆	Municipal	High	361.2	0.82	-7.5	7.2	-16.6	3.2	8.5	25.7		0.0 -14.1	-2.9
IN HANCOCK INCOME	AVG	Corp General	Average	153.7	0.86	-2.6	6.4	-8.9	1.6	9.2	15.3		1.1 -11.2	-0.7
IN HANCOCK INVESTORS	AVG	Corp General	Average	147.5	0.87	-2.8	6.2	-13.1	-0.9	9.4	15.0		6.5 -9.7	-2.0
PER HIGH INCOME	◆	Corp Hi Yld	Very low	209.0	1.55	-3.2	11.8	-3.3	9.4	10.0	8.5		7.6 -7.0	2.7
PER INTERMED. GOVT.	◆	Government	Average	262.6	0.92	-2.6	2.9	-9.2	0.1	8.8	3.1		2.7 -13.1	-5.8
PER MULTI-MARKET INCOME	◆	Multisector	Low	198.9	1.01	-2.2	9.6	-8.1	9.7	10.5	8.4		2.4 -14.1	-6.2
PER MUNICIPAL INCOME	AVG	Municipal	Average	638.6	0.68	-6.5	6.0	-15.7	2.1	8.4	21.2		2.3 -9.1	-2.2
PER STRAT. MUNI. INCOME	◆	Municipal	Low	121.5	0.75	0.2	7.2	-5.6	4.2	7.3	18.2		5.3 -7.6	0.6
INWORT AUSTRALIAN INCOME	◆	International	Very high	74.2	1.43	7.0	7.1	1.0	3.6	9.5	5.2		-4.0 -16.3	-10.7
COLN NATIONAL INCOME	◆	Corp General	High	123.7	1.20	-5.6	5.4	-17.1	4.2	11.1	12.6		14.1 -12.8	-7.3*
TOR INCOME	◆	Government	High	124.4	2.38	-5.4	3.0	-12.1	-3.0	11.8	15.7		1.9 -15.9	-9.5*
S CHARTER INCOME	AVG	Multisector	Average	793.8	0.84	-2.6	6.1	-3.8	3.0	3.0	5.7		-7.0 -15.0	-10.0
S GOVT. MARKETS INCOME	◆	Multisector	High	604.9	0.92	-5.0	3.4	-6.7	0.9	4.4	6.8		-6.1 -15.6	-10.5
S INTERMEDIATE INCOME	◆	Multisector	Average	1321.3	0.91	-3.8	3.8	-9.6	0.6	4.8	7.1		-8.7 -15.9	-10.7
S MULTIMARKET INCOME	AVG	Multisector	Average	881.7	1.14	-3.6	4.8	-2.8	3.0	5.7	9.7		-6.6 -15.7	-10.6
S MUNICIPAL INCOME	◆	Municipal	Very low	324.4	1.31	3.3	6.6	-2.1	6.9	8.1	19.6		10.2 -1.2	5.6
MONTGOMERY STREET INCOME	AVG	Corp General	Average	177.4	0.72	-4.5	6.2	-13.5	1.7	8.6	14.5		-2.0 -14.2	-4.9
MUNICIPAL HIGH INCOME	◆	Municipal	Low	174.3	0.84	-1.2	5.2	-8.2	2.9	8.1	21.3		0.7 -10.7	-2.7
MUNICIPAL INCOME	◆	Municipal	Low	304.9	0.63	-1.9	4.7	-13.7	1.3	6.6	20.8		5.2 -17.4	-7.3
MUNICIPAL INCOME OPPORTUNITY	◆	Municipal	Very low	174.6	1.22	4.3	3.7	1.5	1.8	8.3	21.0		0.1 -13.1	-1.7
MUNICIPAL PREMIUM INCOME	AVG	Municipal	Average	349.1	1.23	-5.9	6.4	-14.5	3.5	8.2	22.9		2.2 -12.9	-1.7
NIENHANCED	◆	Municipal	Very high	461.8	0.68	-8.9	5.6	-19.1	-1.3	8.4	21.6		3.0 -16.3	-5.4
NIINSURED	◆	Municipal	Average	72.7	0.77	-6.5	4.6	-16.9	0.0	6.7	20.8		4.1 -9.8	1.6
NIIVEST	◆	Municipal	Very high	802.3	0.64	-8.4	5.4	-20.2	-2.0	8.9	19.7		2.6 -16.4	-5.3
Y AMERICA HIGH INCOME	◆	Corp Hi Yld	Average	241.6	1.06	-6.6	17.7	-7.8	18.8	13.3	8.6		11.6 -8.0	-2.0
Y YORK TAX-EXEMPT INCOME	◆	Municipal	Low	22.3	0.87	-5.8	4.2	-16.8	4.8	7.0	22.9		16.8 -2.4	6.2
YEN CA MUNICIPAL VALUE	◆	Municipal	Very low	186.9	0.76	-1.8	4.6	-12.8	1.7	7.0	21.6		9.8 -3.3	0.6
YEN INS. MUNICIPAL OPPTY.	◆	Municipal	High	1713.2	0.79	-7.4	6.1	-12.9	0.7	8.1	24.4		-1.2 -11.5	-1.7
YEN INS. QUALITY MUNICIPAL	◆	Municipal	Average	798.4	0.82	-6.2	5.7	-13.5	0.3	7.9	23.9		3.1 -10.8	-1.5
YEN MUNICIPAL ADVANTAGE	AVG	Municipal	Average	906.9	0.79	-4.7	6.1	-12.8	1.1	8.5	23.8		2.8 -8.5	-1.1
YEN MUNICIPAL VALUE	◆	Municipal	Low	1904.7	0.70	-1.6	5.0	-1.6	1.9	7.0	22.1		3.3 -7.9	-0.2
YEN NY MUNICIPAL VALUE	◆	Municipal	Low	119.9	0.84	-1.8	5.5	-7.4	4.1	6.6	23.2		8.7 -4.0	0.1
YEN PERFORMANCE PLUS	◆	Municipal	Average	1236.3	0.79	-2.8	6.1	-13.8	2.2	8.4	23.4		3.8 -11.5	0.5
YEN PREMIUM INCOME	AVG	Municipal	Average	1245.8	0.77	-4.7	4.4	-13.7	-0.7	8.8	23.3		6.2 -9.4	-0.7
YENHEIMER MULTI-GOVERNMENT	◆	Multisector	Average	50.3	1.24	-1.9	4.2	-6.8	-0.1	10.7	13.5		-1.8 -15.5	-6.4
YENHEIMER MULTI-SECTOR INCOME	◆	Multisector	Average	284.2	1.02	-2.8	7.0	-5.2	5.0	10.1	7.8		2.1 -12.0	-0.2
YIFIC AMERICAN INCOME SHARES	AVG	Corp General	Average	133.3	0.72	-3.8	6.6	-12.6	4.2	9.1	15.8		1.4 -10.2	-2.7*
YIRIM PRIME RATE TRUST	◆	Corp General	Very low	720.6	1.22	8.5	7.3	-7.7	NA	7.8	4.6		-0.7 -9.0	-10.7
YNEER INTEREST SHARES	AVG	Corp General	Average	92.3	0.95	-3.8	4.6	-7.6	1.8	9.6	11.5		4.3 -10.1	-2.3
YPECT STREET HIGH INCOME	◆	Corp Hi Yld	Low	129.4	2.30	-2.0	13.7	-2.0	20.2	12.4	7.9		4.7 -11.2	1.0
NAM HIGH-INCOME CONV. & BD.	◆	Convertible	Very low	113.5	1.04	-2.7	15.2	-1.7	14.5	9.7	8.6		8.8 -3.8	2.7
NAM HIGH YIELD MUNICIPAL	◆	Municipal	Average	227.3	0.59	-4.3	6.7	-10.9	4.0	8.7	10.4		11.6 -1.7	7.8
NAM INTERMED. GOVT. INCOME	◆	Multisector	Average	523.0	0.90	-3.4	4.1	-6.5	0.9	8.3	7.2		-5.9 -14.1	-7.7
NAM INVESTMENT GRADE MUNI.	AVG	Municipal	Average	369.6	1.36	-7.9	7.1	-8.4	6.4	8.1	12.2		10.4 -1.7	6.9
NAM MANAGED MUNI. INCOME	◆	Municipal	Average	590.2	1.23	-6.6	7.3	-7.8	6.1	8.0	13.3		8.8 -4.6	3.4
NAM MASTER INCOME	◆	Multisector	Low	448.9	0.95	-3.9	7.8	-7.8	6.4	10.0	6.6		-5.1 -13.2	-9.7
NAM MASTER INTERMED. INCOME	◆	Multisector	Low	306.9	0.92	-4.1	7.2	-9.2	4.6	10.1	6.6		-6.2 -14.5	-11.2
NAM PREMIER INCOME	◆	Multisector	Low	1115.3	0.86	-3.9	7.6	-8.6	5.5	10.3	7.7		-5.5 -15.1	-10.4
OMON BROS. HIGH INCOME	◆	Corp Hi Yld	Average	60.3	1.14	-6.3	NA	-8.0	NA	10.4	7.6		5.9 -2.8	4.6
GMAN SELECT MUNICIPAL	AVG	Municipal	Average	225.1	0.87	-5.5	6.5	-13.1	2.4	8.0	23.3		3.1 -10.9	-1.6
RUS MUNICIPAL CA HOLDINGS	◆	Municipal	Very high	72.3	0.89	-11.3	2.9	-17.7	-2.1	7.9	23.2		12.9 -16.8	-10.2
RUS MUNICIPAL NY HOLDINGS	◆	Municipal	High	103.7	0.80	-9.0	5.5	-19.3	0.9	7.8	20.3		4.3 -14.1	-8.5
CONVERTIBLE SECURITIES	◆	Convertible	Average	234.7	0.80	-6.2	9.2	-7.6	8.8	4.8	9.1		17.5 -2.3	8.2
PLETON GLOBAL GOVTS. INC.	◆	International	High	168.5	1.06	-2.3	2.0	-11.5	-4.0	8.3	9.3		-1.8 -15.0	-8.2
PLETON GLOBAL INCOME	◆	International	High	928.1	0.79	-1.9	4.0	-8.4	-1.7	8.9	7.9		-7.9 -18.2	-11.9
NSAMERICA INCOME	AVG	Corp General	Average	142.0	0.66	-4.5	6.1	-10.6	2.2	9.1	22.7		2.8 -6.6	-4.1
KG PACHOLDER	◆	Corp Hi Yld	Very low	67.5	1.70	1.2	12.7	-6.2	14.3	11.4	7.2		16.0 -4.1	-9.1*
FE INCOME	◆	Corp General	Low	52.4	1.16	-2.5	8.8	-12.0	6.3	9.7	18.7		5.5 -11.0	-4.8
KAMPEN CA QUALITY	◆	Municipal	Very high	213.1	1.62	-11.6	5.3	-18.3	2.8	8.2	23.9		1.3 -12.3	-2.5
KAMPEN INTERMED. HIGH-INC.	◆	Corp Hi Yld	Low	135.9	1.85	-5.3	11.7	-23.1	5.5	17.4	5.8		31.6 -2.1	4.0
KAMPEN INV. GRADE MUNI.	◆	Municipal	Average	75.0	1.47	-8.6	3.6	-11.2	2.3	8.8	21.7		15.5 -1.5	5.7
KAMPEN LIMITED HIGH-INC.	◆	Corp Hi Yld	Low	104.4	1.89	-7.7	11.3	-12.9	12.8	15.7	6.2		24.7 -2.5	4.7
KAMPEN MUNICIPAL INCOME	◆	Municipal	High	423.0	1.28	-9.5	5.1	-10.1	4.9	8.6	18.6		15.7 -1.5	10.0
KAMPEN MUNI. TRUST	◆	Municipal	High	825.3	1.64	-9.6	5.7	-15.0	2.2	8.6	21.9		-0.2 -10.5	-4.0
KAMPEN NY QUALITY MUNICIPAL	◆	Municipal	Very high	129.9	1.66	-9.6	7.2	-15.3	5.2	7.6	19.1		-2.5 -12.6	-4.5
TAUR SECURITIES	◆	Corp General	Average	89.5	1.00	-4.5	4.8	-12.7	0.3	9.2	16.0		0.3 -13.7	-8.7*
X INCOME	◆	Corp Hi Yld	Average	137.7	2.83	-11.2	10.5	-10.2	13.1	14.3	6.3		18.7 -4.5	12.6

of 2/2/95. ** As of 2/1/95. NA = Not available. \$ New fund; less than 12 months' total return.

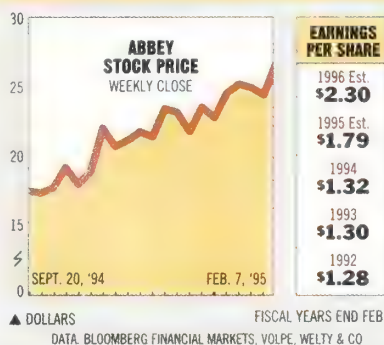
BY GENE G. MARCIAL

LOVE TRIANGLE AT ABBEY

There's nothing like takeover talk to stir things up. And that's what's going on in the home health-care business. The latest buzz is that Abbey Healthcare Group (ABBY)—whose chairman and CEO, Tim Aitken, is a former investment banker in London and New York—is on the block.

"If there's anything to indicate that Abbey is headed toward a deal, it is

ON THE MEND



Aitken's background," says one San Francisco investment manager. "He just wanted Abbey to get back on its feet and get robustly going. And now that that's practically done, he wants to sell off the company," says this pro.

He may be right on the money. A source close to Aitken says Abbey may turn out to be more attractive than some suitors believe. The provider of home medical equipment and respiratory and infusion therapy is said to be considering an offer by a large British pharmaceutical company to buy a 15% to 20% stake. "This foreign drugmaker wants a foot in the door of the fast-growing U.S. home health-care business," says the money manager.

Such a linkage will certainly enhance the value of Abbey, currently trading at 29 a share, to prospective suitors. A source close to Abbey officials says "Abbey is in a kind of a triangle situation right now." It has two avid suitors: Coram Healthcare, which is believed to have talked to Abbey regarding a possible bid for the company, and Homedco Group, a major provider of home health-care services. Coram Chairman and CEO Jim Sweeney says it is his policy not to comment on Coram's acquisition

plans. Homedco didn't return calls.

Homedco's focus is on respiratory treatment while Coram is big in infusion therapy. With estimated 1995 revenues of about \$500 million, Abbey is a key medical-care provider for outpatients. It derives 42% of its revenues from respiratory therapy and 35% from home-infusion (intravenous medicine) and nursing services.

Analyst Ann Logue at Volpe Welty, says Abbey's national reach gives it strength in negotiating contracts with managed-care organizations. The company's contracts have ballooned from 40 in 1992 to 1,400 today nationwide.

Logue figures that, based on earnings prospects alone, Abbey is worth 35 a share. But in a buyout, it could be worth more, she believes.

The price may be in the 45 to 50 range, says one pro, who bases his figures on projected 1995 and 1996 earnings. He says Abbey will likely exceed analysts' 1994 and 1995 earnings estimates. Aitken says he is "pro-shareholder by nature" and would consider any offers. When asked about allowing a British drugmaker to buy a stake, Aitken declined comment. But when questioned on whether Abbey will be sold, he would only say: "At the right price, I would hit the bid."

IT LOOKS LIKE THREE EASY PIECES

Some pros who made a killing with Pet in January, when Grand Metropolitan announced it would acquire the worldwide food producer, have switched their attention to Whitman (WH), a diversified holding company that spun off Pet in 1991. They're convinced Whitman, whose stock has been stuck in the 16 to 18 range for the past 12 months, will be the next buyout winner.

Whitman is in three businesses analysts believe are worth more than what the stock is selling for: Its Pepsi-Cola General Bottler unit produces and distributes soft drinks; the Midas International division provides auto replacement parts and services; and its Hussmann unit makes refrigeration equipment for food-service companies.

Investment manager Mark Boyar, who scouts for companies with assets selling at a substantial discount to estimated intrinsic value, figures Whitman's three units combined are worth 30 a share. He suspects that a number of investors, including Kohlberg Kravis

Roberts, may be looking at Whitman. KKR declined comment.

"These smart and clever operators have the resources and skills to acquire Whitman at its currently depressed price of 16 and then sell off the pieces at much higher prices," says Boyar. Whitman posted sales of \$2.6 billion last year and earned \$1 a share. This year, Boyar sees the company earning \$1.30. Calls to Whitman weren't returned.

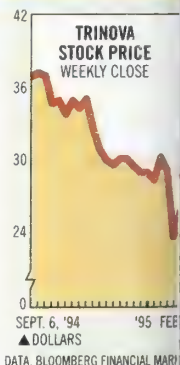
TOO QUICK ON THE TRIGGER?

On Wall Street, 2¢ could cost a stock lot. That was Trinova's (TNV) unfortunate lesson when it reported fourth quarter earnings of 62¢ a share in late January. That 62¢ profit was just a bit below the 64¢ mean estimate that analysts had expected. Wham! Trinova's stock fell 13%, to 25 a share that day. And analysts quickly pulled the plug on Trinova by downgrading its stock and cutting their 1995 earnings estimates. But some bold pros are snapping up shares, now trading at 26.

What's the deal? One New York investment strategist believes a major diversified industrial company wants to buy Trinova, a worldwide maker of a range of industrial engineered components such as pressure hoses and fittings, adapters, and self-sealing couplings. Other products include electronic and pneumatic control devices, and fuel-line components.

One analyst calculates that Trinova is well worth 35 a share in a takeover. The company interested in Trinova is big in aerospace and automotive products—two areas where Trinova derives the bulk of its earnings. Trinova's aerospace and defense-related products generate 28% of profits and 20% of sales. Automotive products, such as body moldings and window frames, account for 52% of earnings and 27% of revenues. Industrial products make up 5% of revenues and 20% of earnings. Trinova posted total revenues of \$1.8 billion last year. Trinova declined comment.

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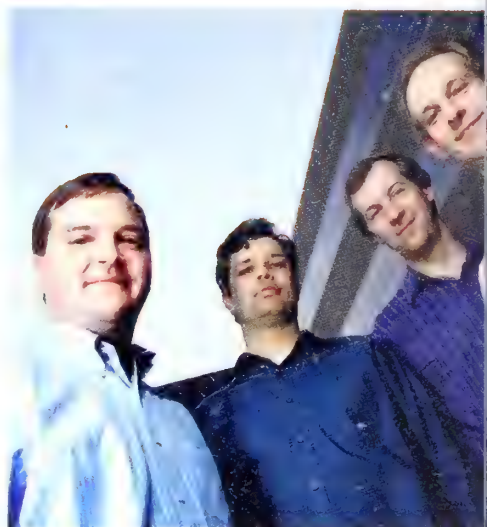
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SEMICONDUCTORS

INTEL: FAR BEYOND THE PENTIUM

But its new chips may be ready before the market is



P6ERS: Perlmutter (second from left) and two other Intel executives.

How fast can an \$11.5 billion company run? Just watch Intel Corp. A year ago, with Advanced Micro Devices, Cyrix, and others nipping at the market for Intel's microprocessors—the brains for millions of IBM-style personal computers—Intel broke into a gallop. The world's biggest chipmaker cranked up production of its new Pentium chip, spent \$150 million on a TV advertising blitz, and chopped prices by as much as 35% per quarter. The latest cut came on Feb. 1, when Intel pruned Pentium prices by up to 40% and fixed the cheapest model at \$273. The result: Pentium sales are growing eight times faster than did sales of the 486 when it was young.

So much for the warmup. The main event is coming on Feb. 16, when Intel will unwrap its sixth-generation chip, code-named P6. By all accounts, this microprocessor is Intel's biggest technical advance since the third-generation 386 was unveiled in 1985. And the P6 is heading to market at an all-out sprint, with small-volume shipments starting

this fall. So the P6 will succeed the Pentium as Intel's most powerful chip in just over two years—a year less than the gap between the 486 and the Pentium.

Can Intel keep up this breakneck pace? Maybe. But from here on, it gets a lot tougher. The P6 is enormously complex. It sports 5.5 million transistors, or nearly twice as many as the Pentium. That poses unprecedented manufacturing and testing challenges, raising the specter of a repeat of the infamous Pentium bug that cropped up last year.

TRAILBLAZING. Intel also must help develop new PC applications that need the power of a P6, such as voice recognition and videoconferencing—plus new top-end systems, from engineering workstations to so-called computer servers. This trailblazing must also pave the way for the P7, which may make its debut as early as 1997 (table). Otherwise, Intel could have trouble persuading PC makers and buyers to

upgrade so frequently. Some PC companies are already dragging their heels. Last year, Compaq Computer Co. Chief Executive Eckhard Pfeiffer killed Intel's ads for implying that the company's chips were nearly obsolete.

For its part, Intel doesn't have a choice—because rivals are picking up the pace even faster. Advanced Micro Devices Inc.'s 486 entry trailed Intel by three years, but AMD will launch its 586-class chip only two years after the Pentium. NexGen Inc. (box) is also selling a Pentium-grade chip, just months behind Intel's. So Intel is prod demand for cutting-edge chips where there's little competition, to protect its fat, 55% profit margins.

The P6 is the first product of Intel's speedup campaign, launched five years ago by Chief Executive Andrew S. Grove in response to growing competition. Intel used to develop microprocessors one after another, every four years. But Grove decided to overlap development cycles. It started the P6 project more than 24 months before the Pentium hit the market. Similar engineers are now years into development of the P7. However, the P7's design took an expected twist last year: an agreement with Hewlett-Packard Co. to forge a "superfast" architecture by melding Intel's

Picking Up The Pace

Intel used to launch development of a new microprocessor every four years. But for the Pentium, the generation gap shrank to three years. And for its P6 and P7 chips, Intel hopes to keep rivals at bay by trimming another year off, despite soaring complexity.

	286	386	486	PENTIUM	P6	P7
START OF DESIGN WORK	1978	1982	1986	1989	1990	1993
FORMAL INTRODUCTION	FEB. 1982	OCT. 1985	APR. 1989	MAR. 1993	Q3 1995	1997 OR 1998**
VOLUME SHIPMENTS	1983	1986	1990	1994	1996	1998 OR 1999**
NUMBER OF TRANSISTORS	130,000	275,000	1.2 MILLION	3.1 MILLION	5.5 MILLION	10+ MILLION**
INITIAL SPEED IN MIPS*	1	5	20	100	250**	500**
PEAK SALES YEAR	1989	1992	1995**	1997**	1999**	2002**
INSTALLED CHIPS	9.7 MILLION	44.2 MILLION	75 MILLION	4.5 MILLION	NONE	NONE

*Millions of instructions per second

**Estimated

DATA: INTEL CORP., DATAQUEST INC., BUSINESS WEEK ESTIMATES

l data-processing methods with HP's
lier reduced instruction-set com-
g (RISC) technology.

ns summing this unlikely marriage
push the P7's introduction into

If so, the P6 would remain In-
prize breadwinner for an extra
—perhaps a bit longer, since the
hybrid Intel-HP design may make
omers more cautious than usual.
his uncertainty means it's crucial
re P6 to inspire customer loyalty.

IN ONE. Technically, the P6 may do
rick. Intel isn't revealing details
ut the chip will crunch more than
million instructions per second
) That's almost double the speed
e fastest Pentium. To pull it off,
P6 actually combines two chips—
microprocessor itself and a special
ory chip that's ultrafast at han-
data. They're bundled in a 2-inch-
e ceramic module. Judging from
ze of this package, the P6 is going
nerate significantly more heat than
Pentium. So, a little refrigerator
g atop the chip may be mandatory,
i could rule out P6 laptops.

chew through software at its
neck pace, the P6 borrows sev-
sophisticated techniques from RISC
ers such as HP, MIPS Technologies,
Sun Microsystems. Like a chess
master, the P6 can look far ahead
software, predict which instruc-
will be processed in what order,
parcel them out in advance to keep
ip's four parallel-processing units
This "dynamic execution" enables
four instructions to be processed
every tick of the chip's internal
—130 million ticks a second in the
P6 model. Still, the P6 will trail the
RISC chips. But Intel insists the
ll outrun its RISC cousins when it
s to PC programs.

el worked on the P6 for an extra
or so because engineers also devel-
a total computer system that ex-
the chip's power. Why? Intel re-
vers all too well having to delay
entium's launch because companion
made by outside chipmakers
n't ready. Intel has since ramped
own production of several key
onents, including motherboards. In
Intel is now among the leading
cers of these circuit boards.

e wanted to make sure we deliv-
the system performance," says
l Perlmutter, head of the P6
t. "We didn't want to give people
r that they couldn't use." Ob-
s Linley Gwennap, a former HP
eer who now edits the newsletter
processor Report: "Intel's taken
processor engine and built a sports car
d it."

sports cars can be finicky. Wring-

THE UPSTART INTEL CAN'T AFFORD TO IGNORE

For years, NexGen Inc. was the
laughingstock of the chip indus-
try. The tiny company bragged
about besting mighty Intel Corp.
with a microprocessor that would
outshine Intel's latest. Year after
year, though, all the startup deliv-
ered was promises—earning it a de-
risive nickname: NeverGen.

Nobody is laughing now. Last
summer, NexGen began shipping its
Nx586 chip. Not only is this the
world's first Pentium clone, it edges
out Intel's speediest chip when run-
ning most software—and yet it's as
much as 27% less expensive. So, lit-
tle NexGen has vaulted more than a
year ahead of much larger Intel clon-
ers such as Advanced Micro Devices

Analysts expect NexGen to sell at
least a half-million 586 chips this
year, vs. 20 million Pentiums for In-
tel. Still, if the chips bring an aver-
age price of \$400, it would mean
\$200 million in revenues.

And the Nx586 is just for starters.
Raza vows to launch a next-genera-
tion 686 chip around the time Intel
introduces its P6 later this year. And
in terms of speed and price, he adds,
"we'll match or beat Intel."

That's the kind of grit that kept
NexGen going during its darkest
days. A native of Pakistan, Raza
joined NexGen as executive vice-
president in 1988, after stints at sev-
eral chipmakers. Then, NexGen's
goal was a finished computer that

would leave Intel-
based machines in
the dust. But
plummeting PC
prices destroyed
that vision by
1991, and Nex-
Gen's \$90 million
kitty—from Com-
paq Computer
Corp. and others—
was all but ex-
hausted. Raza took
over as CEO and
focused on just the
microprocessor. It
was touch and go,
financially. "We
were constantly



NEXGEN'S RAZA: "We'll match or beat Intel"—again

Inc., whose Pentium-class chips won't
be out until fall. The Nx586 can out-
perform a Pentium because it has a
reduced instruction-set computing
(RISC) "engine" and translates com-
plex, Intel-style instructions into sim-
pler RISC instructions that can be
processed far faster. Some 71 person-
al computer makers, albeit small
ones, already offer NexGen PCs.

JUGGERNAUT. Now, the real struggle
begins. This year alone, Intel plans
to spend \$2.9 billion on new chipmak-
ing capacity, and it continues to chop
Pentium prices. Unless NexGen can
persuade some large PC makers to
adopt its chip, it could be crushed
under the Intel juggernaut. "It may
be too little too late," says Silicon
Valley consultant Jeffrey T. Deutsch.

NexGen Chief Executive S. Atiq
Raza retorts that he needs only a lit-
tle piece of the market to survive.

looking over the brink," recalls Raza.
But last summer, IBM began produc-
ing 586 chips for NexGen.

Unlike the Pentium, the Nx586
doesn't have built-in circuits for
"floating-point" calculations. Instead,
an optional coprocessor is required
for heavy math jobs. This actually
proved a boon once the Pentium's
bug surfaced last year. Jim Geer,
general manager at JB Trucking Inc.
in Olympia, Wash., says he bought a
NexGen machine specifically to avoid
getting bitten by the Pentium bug.

Raza promises to net at least one
top-tier customer this year—possibly
IBM or Compaq. Says Rod W.
Schrock, Compaq's director of mar-
keting: "They do have some advan-
tage over the Pentium." The big
question: Is it enough?

*By Robert D. Hof in Milpitas,
Calif., with Peter Burrows in Dallas*

If you're age 40, and want to enjoy your retirement, you've reached this page just in time.

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ing out the bugs in such a complex innovative chip is a forbidding task and supercritical in the wake of Pentium fiasco. "Everybody is going to be looking very closely at the P6," admits Lewis R. Pacely, marketing manager. So Intel has spent extra money on quality testing. But once the dust moves to the factory, says Albert Yu, senior vice-president in charge of microprocessors, "the P6 manufacturing ramp will be very fast."

FINISHED GOODS. Some executives doubt that PC makers will welcome other new chip, just when sales of Pentium systems are surging and 486 machines are still growing in popularity. "Nobody really wants P6 yet," says Stephen Tobak, marketing director for Opti Inc., which supplies computer chips to PC companies.

Buyers could balk, too. Consumers drove the Pentium's initial takeoff because of its multimedia dexterity; they usually keep home electronics longer than two or three years. And businesses, most are still buying machines. "We're just starting to get up to Pentiums," says Michael P. information services director for Arlington Coat Factory Warehouse.

To get buyers on board faster, Intel must expand the puppet-master role it has been cultivating in recent years, encouraging software and PC companies to develop new power-hungry applications, such as multimedia and high-capacity communications, that compete with individuals and businesses to buy the fastest chip. Intel has also developed its own videoconferencing product and networking software.

If its missionary efforts don't pay off, Intel stands ready to seed the market right away. Using its auxiliary parts and motherboard division, Intel can provide the guts of complete P6 systems, so computer makers would only need to snap together the components. Intel could even sell finished P6 machines, since it already builds Pentium PCs for a few outlets and companies.

Just three weeks after the first chips came off the production line in early December, Intel had a new whizzing through Windows programs. Now, it's running animation software and looking virtually as slick as workstations from Silicon Graphics that created *Jurassic Park's* dinosaurs. Rivals had better lace up their running shoes if they want to avoid turning into digital fossils.

By Robert D. H.
Santa Clara, CA

EDITED BY EMILY T. SMITH



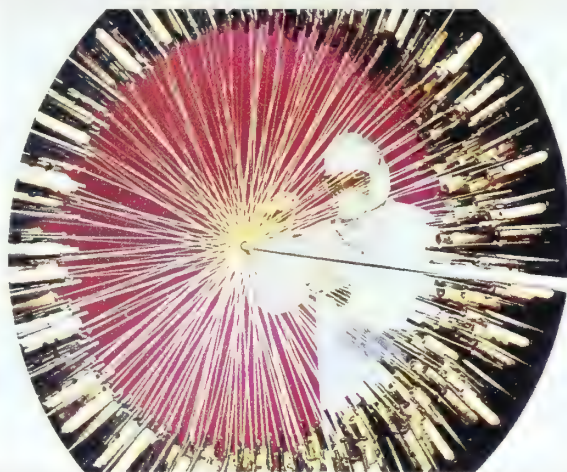
LASERS BLAST THROUGH THE DATA BOTTLENECK?

LE PHONES, FAXES, AND conferencing are creating a flood of information that threatens to overwhelm the circuits that carry that data to distant locales on radio waves. In the future, though, if Thermo Trax has its way, lasers may help satellites transmit more data. Laser light can carry up to 1 billion bits of information per second, far more than radio waves, say executives at an San Diego-based company. Thermo Trax's "pods," which would be added to satellites to receive and send laser beams, weigh just pounds and cost under \$10,000. Lasers are also more secure. Radio waves can spread up to a mile when transmitted, which makes it easier for eavesdroppers to intercept. But the Thermo Trax system can be focused into a beam as little as 1.5 centimeters wide. The tiny beams won't get lost in space because the company has developed a device that helps the satellites align and focus their laser beams on one another. The company tested a prototype last month for a teleconference and plans a test launch during a 1997 military launch. It's also talking to Motorola Inc. and McCaw Communications Inc. about putting pods on their existing satellite networks.

TOUGHER COMPOSITES, THANKS TO BRAIDS

LAMINATED COMPOSITES, USED IN EVERYTHING FROM THE skins of fighter planes to golf-club shafts, have one big flaw: They tend to come apart when the resin holding their layers together cracks under stress. Borrowing from the ancient art of braiding, Albany International Corp. in Albany, N. Y., has come up with a way to make laminated composites stronger. It's common to braid layers of a composite separately, but Albany International goes further by braiding each layer to adjoining ones. Anchored together, they can't slide past one another like cards in a deck—the leading cause of cracking in laminate resins.

The company's Multilayer Interlock Braid technology is starting to find applications, according to the inventor, David S. Brookstein, who remains a consultant to Albany International after becoming dean of the School of Textiles & Materials Technology at Philadelphia College of Textiles & Science. The U.S. Army has used some of the prototype material to build inflatable arches for a portable hangar. And Brookstein says the company hopes to work with a large medical-device company to adapt the process to make a hip implant whose stiffness could be customized.



ANCIENT ART: Albany's machine binds several layers

AN EARLY-WARNING SYSTEM FOR BONE LOSS

YOU MIGHT CALL IT "FRACTALS against fractures." Raj S. Acharya of the State University of New York at Buffalo has developed an improved method for early detection of osteoporosis by measuring the so-called fractal dimension of the bone's honeycomb structure. A bone's fractal dimension is an index of the complexity of its structure.

In osteoporosis, the bone's honeycomb starts to break down. This degeneration shows up as a smaller fractal dimension when a digitized X-ray or magnetic-resonance image of the bone is fed into a computer.

Fractals indicate the onset of osteoporosis long before there is a measurable decline in bone mass—the most commonly used indi-

THIS CONDIMENT ALSO GOES WITH WASTEWATER

HORSERADISH CAN DO A LOT more than merely add flavor to beef. Researchers Jean-Marc Bollage, co-director of Penn State's Center for Bioremediation & Detoxification, and Jerzy Dec, a research associate, have shown that minced horseradish can clean up industrial wastewater contaminated by phenols, toxic pollutants produced from steel and iron manufacturing, ore mining, paper bleaching, and other industrial operations. Better yet, it can do the job just as effectively as conventional chemical and filtering technology—removing more than 95% of the chemicals—but with a bonus: It costs only about half as much.

An enzyme in the plant, horseradish peroxidase, when added to wastewater with peroxide, causes the pollutants to form insoluble polymers. They can then be filtered out and disposed of. The horseradish can be reused as many as 30 times. Researchers are hoping to patent the process and are also experimenting with potatoes and radishes, which contain similar enzymes. One piece of unfinished business: finding ways to dispose of the spent horseradish.

cator of the disease. The associate professor of electrical and computer engineering isn't the first scientist to try measuring the fractal dimension of bone. But he says others had poor accuracy because they used a linear method. He created nonlinear algorithms based on "mathematical morphology," a branch of image processing developed in France to study rocks.

Special Report

PHONE FRENZY

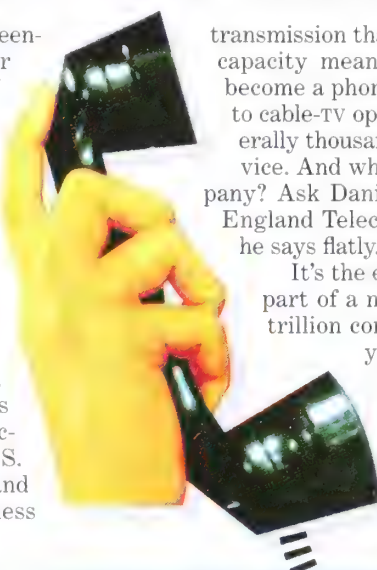
Is there anyone who doesn't want to be a telecom player?

The Area Code Cafe in New York's Greenwich Village may look like just another diner, but it's actually at the forefront of a communications revolution. There's a telephone on every table, and when you order \$5 worth of food, you get a token to make a three-minute call to anywhere in the U.S. The restaurant owns the phones and pays a negotiated rate to a long-distance reseller. Owner Joe Marino says the cafe does not make much of a profit, if any, on the service, but the token gesture is popular among students and tourists who like the idea of bundling a meal and a call home into one service.

What's the significance? The Area Code is just one droplet in a flood of players and services pouring into the rapidly deregulating U.S. telecommunications market. Open markets and technologies such as fiber optics and wireless

transmission that create huge amounts of low-cost capacity mean that just about anyone who wants to become a phone company can. From basement startups to cable-TV operators, energy companies to railroad companies, literally thousands of outfits are poised to offer phone service. And what happens to your trusty old phone company? Ask Daniel J. Miglio, chairman of Southern England Telecommunications Co. "There is no future," he says flatly. "They must become something different."

It's the end of the phone company as we know it, part of a massive restructuring of the country's trillion-dollar communications industry. Everything from your local phone company to Hollywood studios will be affected. While policymakers rush to keep up, dealmakers, entrepreneurs, and executives are preoccupied with the future. Mergers, alliances, acquisitions, entrants, and new services are all changing the telecom landscape.



THE EVOLUTION OF THE PHONE NETWORK

The breakup of the Bell System in 1984 started a process of deregulation that, coupled with new technology, is breaking down the barriers between local and long-distance calls. Companies of all types will soon be able to move into both.

MA BELL

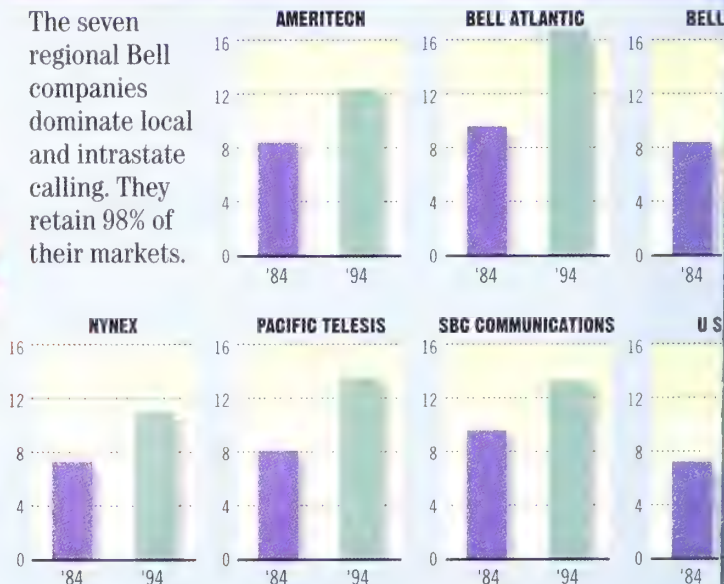


1984

DATA: COMPANY REPORTS; MORGAN STANLEY & CO.

LOCAL CALLING (REVENUES IN BILLIONS OF DOLLARS)

The seven regional Bell companies dominate local and intrastate calling. They retain 98% of their markets.



companies want into cable. Cable operators will sell phone service. Long-distance companies will take on local carriers—and versa. And everyone will seek “convergence”—from electronic yellow pages to e-mail—to lure traffic onto the emerging information Superhighway.

Who will come out on top? At this point, it's anyone's guess. “By the turn of the century, forget which of the companies were long-distance, local, cable, wireless, etc., because everybody will be offering new services, new products, national brands, local niche products,” says Bell Atlantic Corp. Vice President James G. Cullen. Certainly it will be confusing at first, but a decade of deregulation in long distance has conditioned Americans for what's ahead. After all, until 1984 nobody had ever thought about choosing a long-distance company. Today, 30 million Americans a year switch—jumping among AT&T, Sprint, MCI, and others for the best service and prices.

AM BUSINESS. The driving force behind today's phone industry is technology. Most striking is fiber-optic cable. Conventional twisted-pair copper phone wires carry only a few conversations at a time. But a single glass strand can carry at least 32,000 conversations at once. And by beefing up the electronics, AT&T has been able to transmit as many as 20,000. Continuous improvements in both land and wireless technologies promise a steep, steady decline in the cost of communication—analogueous to the way microprocessors have driven down the cost of computers and sparked the personal-computer revolution. Now, new communications technology is bringing forth new ways to deliver a flood of voice, information and entertainment.

Ordinary phone calls, in fact, will be just one of a half-dozen forms of digitized information that can flow across so-called broadband networks (table, page 95). All this capacity means is that a network can handle a virtually

Deregulation and changing technology pave the way for a massive restructuring

unlimited amount of traffic and add new services with almost no new capital investment. “The phone industry is really a dream business. It's the only one where the marginal costs of doing business are zero,” says Harry Newton, a New York telecommunications consultant.

Before the legions of would-be telecom titans cash in on that promise, however, there's still one obstacle to remove: a regulatory framework based on the notion of phone service as a “natural” monopoly. That theory made sense when the system was being created. The undertaking was so vast and costly that it was assumed that only one system could be built. Carriers were granted a monopoly but had to provide universal service—low-cost calling available everywhere.

Since the U.S. broke up the Bell System, deregulating the long-distance market but leaving local monopolies intact, the deregulatory movement has circled the globe. “The idea of the natural monopoly has lost all credibility around the world,” says Ken Zita, a partner with the consulting firm Network Dynamics Associates Inc. in New York. The most recent example: Germany's decision to accelerate deregulation—because the Deutsche Telekom monopoly isn't deliver-

DISTANCE CALLING



1995-2000

Now, cable-TV operators, local- and long-distance companies, and a host of newcomers are racing to compete in multimedia communications.

UTILITY COMPANIES

Why not string fiber-optic wires on those poles?

LONG-DISTANCE PHONE COMPANIES

Local connections will slice access fees

WIRELESS COMPANIES

Gearing up for anytime/anywhere communications

CABLE-TV COMPANIES

Adding phone service could be an earnings boon

GAS PIPELINE COMPANIES

Handy routes for fiber-optic cable

LOCAL PHONE COMPANIES

Deregulation means entry into long-distance and cable TV

LOCAL CALLS

LONG-DISTANCE CALLS

THRUWAY AUTHORITIES

N.Y. may string wires along the N.Y. State Thruway and get into phone service

ALL OTHERS

String wire or resell phone capacity—you can be a phone entrepreneur

ing the prices and services that German businesses demand.

Now, deregulation is about to hit the last U.S. phone monopolies: the \$98 billion local-calling industry dominated by the seven Baby Bells and independents such as GTE Corp.

Special Report

There is virtual agreement in the telecommunications industry, on Capitol

Hill, and in the statehouses that deregulating local service will be a boon to the nation. For proof, look at what happened in long distance. Since 1984, carriers have tripped over each other to add new services, and their market-share battles have sliced rates more than 60%. Competition could do the same in local calling, says Senator Larry Pressler (R-S. D.), chairman of the Senate Commerce Committee: "Progress is being stymied by a morass of regulatory barriers that balkanize the telecommunications industry."

Deregulating this massive industry has implications for the entire economy. Americans dialed up some \$160 billion worth of domestic calls last year, and analysts estimate that the figure will pass \$200 billion by 2000. Lower costs and new services will be a boon to business. And even though many Baby Bells are shedding employees to be more competitive, deregulation should be an overall job creator. An econometric study done by the consultancy WEFA Group Inc.—sponsored by the Baby Bells, mind you—estimates that competition in local calling will spark so much demand for new services that there will be a net gain of 3.6 million jobs by 2003. That's in addition to 1 million phone workers today.

CABLE'S GRASP. When will it all happen? Much depends on Congress. Pressler now leads the effort to replace vintage-1934 regulations. If he can find a compromise between Democrat and Republican approaches, deregulation could begin next year. On the other hand, the legislation could be killed by partisan infighting—as happened last year. Pressler has outlined a bill allowing competitors into local calling immediately but keeping the regional Bell operating companies (RBOCs) out of long distance and cable for one to three years. The Bells want simultaneous entry, while long-distance and cable companies want local carriers shackled until there's measurable local competition.

The market isn't waiting. New players are pushing into local service, and at least 10 states already allow some level of competition in local calling. All but three allow competition on some in-state toll calls. On Jan. 1, Rochester, N. Y., became the first U. S. municipality since 1919 to allow full competition in local residential service (page 97). The rest of the state could follow by August.

You might expect Nynex Corp., the regional Bell, to try to block competition, which will take chunks of its market. But the company is cooperating with New York regulators—because deregulation will let the \$13.3 billion phone giant leap into all sorts of new businesses such as long distance and cable TV. "I'd rather have 10% of the world than 100% of New England,"

says President Ivan G. Seidenberg. Nynex took another big step into the competitive era on Jan. 25, when it announced plans to treat MFS Communications Co., a competitive access provider that links business customers to long-distance carriers, as a co-equal common car-

WIRELESS WONDER
GTE has a cordless phone that turns into a cellular phone when you leave the house



COMPETITIVE FERVOR "I'd rather have 10% of the world than 100% of New England"

— NYNEX PRESIDENT IVAN G. SEIDENBERG

rier. It's the first such pact between an RBOC and a

MFS, a pioneer eight years ago, is about to get plenty of company. Within a few years, consumers may start getting phone bills from cable-TV operators, utilities, or wireless carriers. They could even get service from a totally unexpected type of provider—such as the New York State Thruway Authority. It's gauging the feasibility of laying fiber-optic cable along its rights-of-way and offering phone service

It's not so far-fetched. Deregulation brought nearly 20 new entrants into long distance. Wiltel Communications Systems, now part of LDDS, the No. 4 long-distance company, got its start by running fiber along the Williams Cos. pipelines. Anyone with a right-of-way could do the same. In Britain, 12 electric companies created Energis, a 2,000-mile fiber-optic phone system. New Jersey's Public Service Electric & Gas Co. is developing a system with fiber to read meters and offer appliance management, home security, and medical alert services. New Orleans-based utility Entergy Corp. is testing a similar network in Chenal Valley, Ark. These systems could just as easily double as phone lines.

While some players putter, cable-TV operators are plunging in. They own wires that reach the homes of 59 million Americans, and phone service looks like a no-brainer. Time Warner Inc. executives are expecting an extra \$10 per customer each month, and Morgan Stanley & Co. calculates that phone services should add 8% to 10% to a cable system's value. Also, coaxial wiring can handle broadband speeds right away, so it will be cheaper for cable

Even the New York State Thruway Authority is weighing the idea of laying fiber-optic cable along its rights-of-way

es to add voice than for phone companies to add video. a huge competitive advantage," says Glenn A. Britt, dent of Time Warner Cable Ventures.

me of the nation's top cable-TV operators—Tele-Communi- ons, Cox Enterprises, and Comcast—have formed an ce with Sprint to build and operate a nationwide wire- phone network. The group is the top bidder for licens- operate a new form of wireless phoning known as per- communications services (PCS), betting \$1.4 billion so

at the new technology can fill gaps ational network. Regulations per- ing, the group will offer one-stop ing for local calling, long distance, ar, PCS, and cable, says Sprint -Distance President Ronald T. y. "We have the chance to offer thing that's

the market **INTERACTIVITY** now," says An AT&T gizmo can transform your TV into an answering machine/banking/shopping terminal

e across New York and Ohio. California regulators say let cable operators offer telephony as soon as any phone ny in the state receives approval to offer TV. e confusing blur between cable and phone operators is ional: Executives in both industries say their futures epend on it. "We're going to be an integrated commu- ns company with telephony, video—which is our -and new products: interactive audio and video prod- says William T. Schleyer, executive vice-president of -based Continental Cablevision Inc. "If you don't make ove, you'll have trouble competing in the future. If all o is play defense, you have no defense."

MAKING. You don't have to tell ls. U S West Inc. is furiously ioning itself for video, pay- .5 billion for 25.51% of Time r and launching video-on- d trials. U S West, Bell Atlan- llSouth, Ameritech, and Nyn- e all won federal court rulings g them to provide video over lines, also known as video e. On Jan. 29, a federal court he same right to most of the 's small phone companies. The next phase of the wireless is another Bell challenge. RBOCs have profited hand- from their cellular holdings, industry has streaked to its t \$12 billion level. But PCS ing dozens of rivals. The FCC as have attracted hundreds of s, ranging from the Baby on one-person startups to cel- laycoon Craig O. McCaw, who l more than \$300 million for s in New York.

Why the scramble? PCS, using higher frequencies and small- er "cells" than cellular, holds out the promise of low-cost phones for use around a town or building—a possible rival to the wired local phones. A study by BIS Strategic Decisions pro- jects that some 77 million U. S. subscribers would consider using a wireless service to replace or upgrade their existing home phone if it were the same price.

In addition to attracting new players, phone frenzy is inspiring a swirl of joint ventures and acquisitions. Worldwide mergers and deals among communica- tions, information, and entertainment companies hit a record \$27.8 billion last year, according to KPMG Peat Marwick. "If the phone companies want to stay profit- able they'll have to offer multiple ser- vices," says Jeffrey Miller, a telecommuni- cations specialist with Andersen Consulting. "But that's going to require a big investment, and they don't necessar- ily have to carry the whole weight on their own."

"TELECOMPUTER" COMPANIES. Deals now cross every industry line. Pacific Telesis, Bell Atlantic, and Nynex have formed a joint venture with Hollywood superagents Creative Artists Agency to develop new



multimedia programming, while Ameritech, BellSouth, and SBC have joined up with Walt Disney for the same purpose. "We've got to make sure we have access to programming," says Ameritech Corp. Chief Executive Richard C. Note- baert. That's why Nynex has invested \$1.2 billion in Via- com, while SBC Communications Inc. (formerly Southwestern Bell) has paid \$650 million for the Hauser Communications cab- le system in Maryland and U S West has teamed with Time Warner. "Entertainment and information, we believe, is the wave of the future," says U S West Vice-President for Strategy Development Chuck M. Lamar.

The biggest spender is AT&T. In addition to its \$12.7 billion

SAY THAT AGAIN?

Here are some of the terms you'll need to know as new calling choices multiply:

ACCESS LINE The circuit that connects a customer to the telephone network.

BANDWIDTH The range of frequencies that can be transmitted. The greater the bandwidth, the greater the capacity.

BROADBAND A fuzzy term describing high-bandwidth connections—generally those that can carry numerous voice, data, and video channels simultaneously.

COMPETITIVE ACCESS PROVIDER (CAP) An alter- native to the local phone company.

COMMON CARRIER A company offering telecommunications to the public on a nondiscriminatory basis.

INTERACTIVE Refers to the ability to carry two-way transmissions. Phones are interactive. Cable TV is not—yet.

MULTIMEDIA NETWORK A system that can carry several forms of communications, among them voice, data, and video.

NUMBER PORTABILITY Lets a customer retain the same number when chang- ing carriers.

PERSONAL COMMUNICATION SERVICE (PCS) A digital wireless service that might be inexpensive enough for full-time local calling.

RESELLER A company that buys trans- mission services at bulk rates for resale to the public for a profit.

SPECIALIZED MOBILE RADIO (SMR) A two-way, radio-dispatch service being upgraded to provide cellular-like phone services.

VIDEO DIAL TONE An automatic connection to a network transmitting video.

Special Report



REINVENTION

Bell Atlantic is racing to develop multimedia systems as well as programming

ester Telephone Corp. capital

The specter of hundreds of competitors where once there were none has energized Baby Bells to turn efficient. Until the past year or two, had little incentive to cut costs. Most states capped rates at a determined profit level, and half still do. Nynex, the tightly regulated Bell, is all a rate of return on assets. New York of only 9.15%—thing more is returned to customers in the form of rate cuts.

Now local phone companies have plenty of motivation in addition to competition for

purchase of McCaw Cellular Communications, it has bought into a string of technology startups, including game makers 3DO and Spectrum Holobyte and software publisher Knowledge Adventure. It's one of the big backers of General Magic Inc., which provides the software for the phone giant's new PersonaLink messaging system. "We've come to the gradual realization that we can't afford to do everything ourselves," says AT&T Chairman Robert E. Allen.

Computer giant IBM doesn't want to be left out, either. It flirted with telecom in the 1980s and got burned. But with communications and computing merging, it can't afford to sit this one out. IBM already operates the world's largest data network and resells voice services to some customers. John M. Whiteside, general manager of IBM's Global Network, says the company won't compete with voice carriers but will sell customers services to conduct electronic commerce. As he puts it: "It's the birth of the telecomputer company."

FIBER GLUT. What will all this bring to consumers? For a glimpse, visit Bell Atlantic's \$200 million so-called "digital factory" in Reston, Va. There, the company is devising a system to deliver movies on demand, home shopping and banking, interactive programming, and information services to TVs over copper phone lines—all without interfering with regular calling. Up at AT&T in New Jersey, engineers have a gadget to turn your TV into an answering machine/home-banking/interactive-shopping terminal. GTE Corp. has a cordless phone that turns into a cellular phone when you leave the house. BellSouth Corp. is pushing personal digital assistants that send and receive E-mail, faxes, and voice calls wirelessly.

The new telecom world won't just be big companies with whizbang techno-goodies. A glut of fiber capacity has created a bonanza for entrepreneurs. Anyone who can make a deal with MCI Communications Corp. or AT&T to buy capacity at bulk rates can become a reseller. Former dental hygienist Kathy Haycock, 43, mortgaged her home to start Call-America, an AT&T reseller, in Mesa, Ariz. "No one would give me a loan because they thought it was crazy," she says. Now, she has 25 employees and 20,000 customers. Deregulation should bring reselling to local calling, too. In fact, in Rochester, rivals will start by leasing Roch-

calling, they could face a sharp reduction in their most lucrative business: the access fees they collect from long-distance carriers. Those fees totaled \$30.8 billion in 1994, some of the RBOCs' total revenue—and more than 40% of the distance carriers' expenses.

Deregulation will change that. The Bells expect to get long distance, but long-distance carriers also expect to get into local service—in part to slash access fees. Each of the big three of long distance is preparing direct local connections—Sprint through its cable consortium, AT&T through McCaw, and MCI through a bypass network planned to start businesses in 200 cities within five years. It will be worth \$2 billion cost, says MCI President Gerald H. Taylor. "Access, cut access, cut access, that's what it's all about." Executive Vice-President Alex J. Mandl says the phone will try any form of local access—wireless, cable, building own local loops, even reselling Bell service. "We must have as many links to the customer as possible," he says.

Can the Baby Bells thrive amid all this competition? Or will they be mere victims? "It's a wake-up call," says SBC Executive Vice-President James R. Adams, who has glimpsed the future in Britain. There, SBC is part of a cable-TV joint venture in which 60% of the 1.3 million subscribers use the cable

system for local phone calls. The way he sees it, SBC's cable unit "is the hunter, and we're the hunted.... We just have to make sure we're not the easiest deer for our rivals to find."

All the local phone companies are fully trying to look less like prey. They're spending billions to create stronger brands and build broadband networks. British Telecommunications plans to spend \$16 billion over the next five years; Bell Atlantic has budgeted \$1 billion; U S West \$10 billion; Southern Bell \$4.4 billion.

The Bells are also investing in new management talent. Two years ago, Ameritech hired 40-year-old James Firestone away from American Express Co.'s Travelers Group to run its residential business. A quarter of Nynex' executive staff has been hired from outside the phone business, mainly to boost marketing. It's an important step toward the day when customers will have a local service choice, says Seidenberg.

Long-distance companies are itching to get into local service—and pay lower fees to the Baby Bells

ation to our customers is to get on with the change." Such sentiments are becoming the norm rather than the exception among Bell execs. And why not? Despite the risks, regulation has been, above all, a boon to phone companies. The International Telecommunication Union notes that in every market where competition has been introduced, rates have fallen and calling volumes have risen dramatically. Just consider AT&T: It has lost 40% of its market share and dropped rates by 60% over the past decade—and it's doing better than

ever. Revenues for 1994 jumped 8.3%, to \$75.09 billion, equal to its predivestiture level, while operating profits soared 26%, to \$4.71 billion. "The people who are worried about their slice of the pie today are goofy. They should be worried about expanding the pie," says Southwestern Bell Mobile Systems Chief Executive John T. Stupka. If they're not convinced, they should stop by the Area Code Cafe for a token.

By Catherine Arnst in New York, with Kevin Kelly in Chicago, Peter Burrows in Dallas, and bureau reports

THE NEW ERA BEGINS IN ROCHESTER

Competition in local phone service is more than just a dream in Rochester, N.Y. On Jan. 1, it became the first U.S. city in 75 years to allow residents a choice of local carriers. Rochester Telephone Corp. is as any and all comers connect to its network and its customers. The reward: an end to Rochester Tel's state-mandated profit limits and the right for it to offer long-distance and local services. The agreement makes the Great Lakes community of 1,000,000 a test bed for the telecommunications battle to come. Granted, the change is not much evidence yet. Time Warner Cable, the local cable company, has set up booths in malls around town to push a new cellular service, and AT&T is trying out a direct-mail campaign to sign up customers for local calling. Other potential competitors are entering the market. But consumers aren't dashing out to change carriers. "I'm not really sure what's going on out there," says Valerie Huff, a high school math teacher. "Nobody's really talking about it."

CAPEE. Why Rochester? Mainly because Rochester Tel is not a Bell. Founded in 1899, it managed to avoid joining the rest of the Bell system and so escaped the many restrictions placed on the regional operating companies when AT&T was broken up. As a result, Rochester Tel—now reorganized as the local service arm of the Frontier Corp. holding company—has always been able to offer long distance outside its service region. It is the seventh-largest long-distance carrier and owns 34 other local phone companies in 13 states, making it the 12th largest local-phone company. But it was still restricted from earning more than an 11% rate of return by the New York Public Ser-

vice Commission. So Rochester Tel proposed ending its monopoly in return for an end to profit caps and freedom to compete. It agreed to cut rates 11% and freeze basic residential fees for seven years. Customers can keep their phone numbers if they switch carriers, and competitors must be allowed to connect seamlessly to the local network. Frontier Chairman Ronald L. Bittner says he's delighted. "We figured the worst form of competition is regulated competition," he says. "Besides, we had an ulterior motive. We figured the market would

offer cut-rate prices and still make a profit. "It's an interesting experiment, but naive," he says. Still, an AT&T spokeswoman says the company so far is doing "better than expected" in its first month back in the local phone market.

NO MAGIC WAND. Rochester Tel admits its model isn't perfect. "I empathize with AT&T's position," says Jeremiah T. Carr, president of Rochester Telephone. "You can't just wave a wand and have the local monopoly go away... I can't deny that customers won't think of us first."

Time Warner is determined to



expand and we'd get a larger share, including other carriers paying to use our network."

It does look like a win-win situation initially. Until their networks are built, competitors will simply resell Rochester Tel service. That bothers AT&T. "It's a bad model because the customer doesn't really have any [network] choice," complains Joseph Nacchio, head of AT&T's consumer calling business. Rochester Tel, he says, is charging resellers 95% of its retail price, giving little room to

make Rochester more than an experiment. It has some 200,000 cable customers there and is upgrading its network for telephony. "We'll have dial tone by the third quarter some-

time," promises Glenn A. Britt, president of Time Warner Cable Ventures. Then, the competition will really begin. Is Rochester Tel a little worried? Well, allows the silver-haired Bittner, "I used to have dark hair."

By Catherine Arnst in Rochester, with Michael Oneal in New York

EDITED BY AMY DUNKIN

HOW TO EXERCISE A BOOMER BODY

In her younger years, Jacqueline Hamilton, a corporate art consultant in Houston, played tennis or swam whenever she was so inclined. But she says middle age brought an end to purely spontaneous exercise. "I started to feel stiff. My back and hips were hurting," says the 53-year-old Hamilton. And that made it difficult for her to jump back into physical activity after a hiatus: "I realized my body was getting older and [that] I'd better use it or lose it."

Today, spurred by her gynecologist and readings on fitness, Hamilton follows a regular routine, stretching first and then biking, swimming, or walking almost every morning. Her aches and pains have diminished, and her body "just works better," which she says makes her feel younger. "If you exercise only when you feel like it, you're going to feel your age," she says.

TICKTOCK. Indeed, doctors and physical therapists agree that a consistent exercise program can ease and even minimize the effects of aging, especially after 40. Dr. Lewis Maharam, a New York sports-medicine specialist who writes a monthly health column for older athletes in *Masters Sports Newsletter* (800 562-1973), says: "Routine exercise is the best way to slow down the aging process.



HEALTH AFTER 40 Vary routines and stretch, stretch, stretch

It lengthens and improves quality of lives."

That's the good news. The bad news is that physical activity will not stop the clock. Bodily degeneration is a biological fact of life, and most people feel its effects acutely

during middle age. Necks and backs start to ache inexplicably, impromptu one-on-one basketball games result in days of muscle soreness, and a persistent twinge in the knee makes that last mile of what used to be an easy jog

completely that the bones it to connect and cushion together.

Similarly, muscles become shorter, tighter, more resistant to change, and less flexible. Strains and tears consequently more com-

seem an almost inevitable strain. "I see a lot of middle-aged people who are frustrated that they can't do what they used to do," says Dr. Terrence Glenn, director of Medifit, a man Performance Rehabilitation Center, a division of Baylor College of Medicine in Houston. "I tell them it's natural, that it's part of getting older, but it's hard for them to accept. Human nature is rough."

LESS RANGE. The loss of range of motion for middle-aged people, Glenn says, is a natural part of understanding the changes going on in their bodies and, like Hamilton, alter their exercise programs accordingly. Otherwise, they're speeding up their bodies' decline. After 40 years of use, joints naturally are stiffer and less pliable. Viscous cartilage becomes drier and increasingly brittle. Range of motion decreases, and predictably, a person in middle years is more apt to suffer from knee, hip, and elbow pain. Midlife is also the time when most people first experience arthritis, which occurs when the cartilage wears away so

plus. Oxygen levels in tissues also tend to drop, resulting in reduced performance and a slower aging rate.

Even these grim realities, what to do? Fear not. A zipper sweater, lap and Barcalounger are prescribed. Rather, a moderate muscle stimulation is especially important. Glennon and other experts recommend instead of engaging in grueling work, middle-aged individuals exercise for 30 minutes—not three or four a week, but at least to consistently loosen aging tissues. Aerobic exercise gives the most benefits. Anaerobic conditioning—such as weight lifting—is a good supplement for toning and shaping legs.

To prevent injury, be sure to stretch muscles before, during, and after exercise. This will help to maintain youthful flexibility, promote oxygen flow, reduce strain on joints. Periodic stretching throughout the day is also a good idea—especially for deskbound. Take time out to do a few shoulder and neck rotations, calf extensions and twists at the waist. Additionally, fitness experts advise varying exercise activities to preserve tone and strength in all muscle groups. Ensure that the same muscles and joints are not exercised every time. Douglas Kelsey, a researcher, physical therapist, and rehabilitation specialist in Austin, Tex., advocates cross-training as particularly beneficial to the 40-plus crowd, because “cumulative wear is what causes the body to break down.” But do not switch activities every week. Kelsey suggests picking a sport or workout program and repeating it regularly for months before changing. After another two months, return to the original regimen, or on.

Help For Staying Fit In The Middle Years

ORGANIZATIONS

The American Academy of Anti-Aging Medicine 1510 W. Montana, Chicago, Ill. 60614, 312 528-1000. Hosts a yearly anti-aging conference and sells videotapes of the proceedings; also makes physician referrals.

The American College of Sports Medicine P.O. Box 1440, Indianapolis, Ind. 46206-1440, 317 637-9200. Offers a free brochure, *Fit Over 40*, to those sending a self-addressed, stamped business-size envelope; also publishes a quarterly newsletter called *Fit Society* (\$20 per year).

The American Running & Fitness Assn. 4405 East West Highway, Suite 405, Bethesda, Md. 20814-4535, 800 776-2732. Provides free materials on fitness, publishes a monthly newsletter called *Running & FitNews* (\$25 per year), offers over-the-phone advice and referrals.

BOOKS

Biomarkers: The Ten Determinants Of Aging You Can Control by William Evans and Irwin H. Rosenberg (Simon & Schuster, \$12)

Fit or Fat by Covert Bailey (Houghton Mifflin, \$5.95)

How and Why We Age by Leonard Hayflick (Ballantine Fawcett, \$24)

Power Foods: High-Performance Nutrition for High-Performance People by Liz Applegate (St. Martin's Press, \$12.95)

Stretching by Bob Anderson (Random House, \$12)

The "E" Factor by Dr. Bob Goldman (William Morrow, \$24.95)

Therapists and physicians alike urge their middle-aged patients to engage in more low-impact sports such as walking, swimming, and biking. High-impact activities such as running and tennis are far more traumatic and wearing on bones, muscles, and joints. When pursued unrelentingly, they abet and even accelerate the body's natural degeneration.

TALK OR SING? Middle-aged individuals should also remember that their cardiovascular systems are not what they were 20 years ago. The heart, like all muscles, weakens over time. On average, the maximum heart rate decreases 10 beats per minute every decade. Even worse, blood vessels become more rigid and, depending on a person's diet, may develop plaque deposits. Those ob-

structions, along with diminished heart-pumping capacity, slow circulation.

That's why exercisers in midlife should have a physician reassess their cardiovascular health yearly—regardless of fitness level. “No one, not even the greatest triathlete, should be lulled into thinking that because they are in shape, they won't have a stroke or heart attack,” Maharam says. “Many cardiovascular problems are just plain hereditary, and that is something you need to pay attention to—especially after 40.”

To safeguard the heart while deriving benefit from a fitness program, individuals should raise their heart rate to 75% of their maximum. The maximum heart rate is generally 220 minus a person's age, but individual health issues may lower the

upper limit or “safe zone.” How much is too much? Kelsey says an easy way to know if you are exercising with appropriate intensity is the talk/sing test: “You should be able to talk but not sing while you're exercising. If you can sing, you're taking it too easy. If you can't talk, you're going too hard”—which means the heart is beating too fast.

NO BLAHS. Finally, age brings with it a slower metabolism. Calories are not burned as efficiently or quickly, and thus feelings of sluggishness and incremental weight gain of up to a pound every year is normal. That's why frequent exercise, which speeds the body's metabolism, is crucial after age 40 to counteract the blahs as well as age-induced weight gain.

Unfortunately, a high-fat diet can cloud the results for even the most dedicated exerciser. That's because the fat from those cheeseburgers and chocolate shakes that you've enjoyed since college is less easily burned in the middle-aged body—and more likely to take up residence in tummies, hips, and thighs.

So Glennon warns the middle-aged not to use their girth—or lack thereof—to gauge the success or failure of their exercise programs. “They could be getting wonderful benefits musculoskeletally, cardiovascularly, and even psychologically from their programs but get discouraged because their waistline may be very slow to change,” he says.

In fact, the consensus among physical medicine professionals is that an exercise program's true measure of success is the fun factor. If an activity is fun, there is more incentive to keep doing it. And if you've reached middle age, aren't you entitled to some fun? *Kate Murphy*

PROSTATE CANCER: IS THE BLOOD TEST WORTH IT?

Shortly before financier Michael Milken was released from prison in early 1993, he had a thorough physical exam and was pronounced healthy. But Milken, 46, had lost a friend to prostate cancer. So he asked the doctor to perform a blood test he had heard about which measures PSA, or prostate specific antigen. His internist didn't recommend the test for a man so young, but Milken insisted. When the test showed Milken had very elevated PSA levels, he consulted a urologist, who found Milken had an aggressively growing cancer.

Prostate cancer is now the No. 2 cause of cancer deaths in U.S. males. Some 200,000 men will be diagnosed with the disease this year, and almost 40,000 will die of it. On its face, Milken's story suggests PSA should become part of a routine battery of can't-hurt annual screening tests for healthy middle-aged men. Plus, a recent study in the *Journal of the American Medical Assn.* validated the test's ability to find the majority of prostate cancers. But a growing minority of doctors are not convinced PSA screening should, in fact, be routine.

SLOW GROWTH. Here's what's going on: Until the PSA test became available several years ago, prostate problems were typically discovered when a man developed symptoms, such as trouble urinating, or when a physician detected an abnormal prostate during the infamously "digital-rectal exam."

(For this procedure, the doctor inserts a gloved finger in the rectum to check what should be a walnut-size gland located just beneath the bladder.) But stories about well-known prostate cancer patients such as Milken, Senator Bob Dole (R-Kan.), and the late Time Warner Chairman Steve Ross, are prompting scores of middle-aged men to demand PSA screening tests—even when they are symptom-free.

Urologists and internists

One reason for the dispute over PSA testing is that prostate cancer is often slow-growing—so slow that most men who develop it actually die of something else. Unfortunately, PSA levels don't always distinguish the slow-growing form from a more aggressive disease that should be treated immediately. It will help if scientists succeed at current efforts

to develop a test to flag the more virulent form. But the screening issue will remain controversial until a crucial question is answered: Will early detection by PSA and subsequent intervention lower the death rate from prostate cancer? A huge study launched by The National In-

tervention Group, which is testing whether PSA testing and procedures with various side effects that include incontinence and impotence. "Do you want to enter this loop when the chances of being a false positive are very real?" he urges patients to ask themselves potential complications are just physical: Some men become obsessed with getting surgery.

might be better treated with watchful waiting.

SIDE EFFECTS. Urologists such as Peter Carroll, associate professor of medicine at the University of California at San Francisco, say they believe early identification and treatment will bring death rates down.

But Carroll also acknowledges the uncertainties and men not to overlook to unusual cases as Milken's. He believes men must be fully informed of the probabilities of side effects associated with treatment and make decisions based on their own situations. For example, men in their 40s are so unlikely to develop a prostate cancer that will kill them, many urologists tell them not to

Help Making Tough Choices

Confused about whether to take the prostate specific antigen test? Here are resources for men concerned about prostate cancer:

THE AMERICAN CANCER SOCIETY 800 227-2345 Sponsors prostate cancer support groups for men called Man to Man and groups for men and their partners called Side by Side; for local organizations, call local ACS chapters

THE AMERICAN FOUNDATION FOR UROLOGIC DISEASE 800 242-2383 Has a Prostate Health Council and Prostate Cancer Support Network that can provide general information about the disease and ongoing research

US TOO INTERNATIONAL 800 808-7866 Coordinates support groups in most major cities and publishes a quarterly newsletter, *The Prostate Cancer Communicator*, addressing treatment options and psychological and social aspects of prostate cancer

alike agree that men, usually starting in their 40s, should have a yearly rectal exam. Those with symptoms or detectable prostate nodules should receive a full work-up, including a PSA test. Many urologists cite cases such as Milken's as justification for routinely checking PSA during annual physicals, much the way gynecologists order mammograms and Pap smears for adult women. Their hope is to catch prostate cancer early enough to cure it or at least slow its progress. Treatments include radiation, chemotherapy, hormonal therapy, surgical removal of the prostate, and other new techniques.

stitutes of Health should answer that question, but the results won't be clear for a decade or more. Until that's resolved, one fear is that doctors may simply be identifying incurable cancer earlier, then doing procedures that lessen the quality of the patient's remaining years.

Internists in particular worry that routine PSA screening will frighten huge numbers of men for no purpose. The JAMA study, for example, showed false positives in 10% of the healthy men tested. White River Junction (Vt.) internist H. Gilbert Welch, an expert in early detection, notes that a positive PSA test often results in fur-

er with PSA. But an 80-year-old married man with a family history of prostate cancer must weigh factors.

Prostate cancer information and support groups helping men sort through these quandaries: There can talk to others who have made—and now are making—these tough decisions. A number of books are available, too, such as *Prostate Cancer: Making Survival Decisions* by Sylvan Meyerson and Seymour Nash (University of Chicago Press, \$19.95). They may raise issues you can discuss with your doctor before taking a test. *Joan O'C. Harte*



IE MEDICAL HOT LINE YOUR PC

1990, Gary Schine
diagnosed with
cell leukemia, a
and supposedly

able cancer. Schine,
3, refused to accept his
gist's prognosis at face
Instead, the writer
consultant researched
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arned of clinical trials
experimental drug
as 2-CDA. Schine be-
one of the first to re-
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Today, he jogs two
day and is by all indi-
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er, he can search in just over
an hour what it took him
two weeks to uncover more
than four years ago.

SUPPORT GROUPS. But you
don't have to be a profession-
al researcher to ferret out
health data online. In fact,
anyone equipped with a PC
and modem can mine a
wealth of diverse medical,
health, and fitness informa-
tion. Although a good deal is
med-speak aimed at health
professionals, you can find

lots of rich material that lay-
people can understand. The
information may be of particu-
lar value to aging baby
boomers as they become
more obsessed with their de-
clining bodies.

For starters, the major on-
line services
such as Amer-
ica Online, CompuServe, and
Prodigy provide health news
and offer medical and health
support forums where users
can tap into libraries, ex-
change messages, and com-
miserate in real time about
common problems. The Unit-
ed Cerebral Palsy Assns. and
National Multiple Sclerosis
Society are among the organ-
izations represented on AOL.
Prodigy features general arti-
cles on wellness, exercise,
sports, and other subjects in

its Health Topics section.

CompuServe has especially
meaty offerings—although
you'll sometimes pay hefty
charges of up to \$24 an hour
above the service's regular
connect charges. Besides ded-
icated cancer, diabetes, mus-
cular dystrophy, and holistic
health forums, CompuServe
members can tap into the
Physicians Data Query from
the National Cancer Institute,
which includes information on
cancer types and treatments.
The Rare Disease Database
offers resources and drugs for
“orphan” diseases affecting

HEALTH AFTER 40

fewer than
200,000 Ameri-
cans. In Knowledge Index,
you can find the full text
from more than 50,000 jour-
nals. You can also reach Med-
line, a biomedical database
with more than 7 million re-
ferences and abstracts culled
from some 4,000 medical jour-
nals by the National Library
of Medicine.

Those without a Compu-
Serve membership can still
tap into Medline. One way is
with \$30 software called
Grateful Med, available from

National Technical Information Service in Springfield, Va. (800 423-9255). Another is via PaperChase, a service of Boston's Beth Israel Hospital. You can reach PaperChase by phoning 800 722-2075 or using the Internet tool "Telnet," a method of connecting to a remote computer on the Net (Telnet to pch.bih.harvard.edu). PaperChase can also connect you to separate AIDS, health-planning, and cancer databases. Searches can add up, though: Rates are \$23 per hour.

Hundreds of specialized electronic bulletin boards cover the vast medical landscape as well. The Black Bag BBS in Collegeville, Pa., contains the latest news from the Food & Drug Administration and on AIDS treatments, among others. Among Black Bag's topic areas are smoking and cancer, and pediatrics. In the smoking section, for example, you can read tips on quitting. People who dial in can download a list of other health-related bulletin boards, compiled and updated by Dr. Edward Del Grosso, a radiologist who checks out each board he includes. You can also get the list through the Internet by sending E-mail to lists@black-bag.com. Or check the January issue of *Boardwatch Magazine* (800 933-6038).

SHROUD OF PRIVACY. Not surprisingly, the Internet is a vast reservoir for medical and fitness information. In January, the Centers for Disease Control & Prevention announced the availability of *Morbidity and Mortality Weekly Report* and other CDC publications online. Written for medical professionals, *MMWR* reported the first AIDS cases in 1981 and the outbreaks of Legionnaires' disease and hantavirus. You can find the reports by sending E-mail to lists@list.cdc.gov or

by using a World Wide Web browser such as Mosaic to connect to the CDC. Meanwhile, the National Cancer Institute is among the outfits putting together a World Wide Web server over the Internet.

Why are so many people seeking online medical counsel? For one thing, it's smart consumerism. Many patients believe their doctors are not always abreast of the latest medical literature. By uncov-

them on their problem." The board is reachable by modem at 800 644-2271.

Given its far-reaching scope, the online community provides patients with rare conditions a link to others who share their disorders. Patients with more common maladies can also gain confidence by chatting with people who have been through it all before. Says one woman who went ahead with knee surgery after comparing notes

when they log on. Her Source's modem number is 813 979-7307.

But just as others know who you are, you have no way to determine the credentials or expertise of persons providing medical advice. To some extent, bulletin boards and online services are self-policed. Those surfing the boards would be wise to pay attention to the disclaimers posted when you sign on.

You may encounter well-intentioned people who pass along wrong information. Others may be trying to sell something.

"POND SCUM." Ira Lerner, a registered dietitian, recently checked out some of the food on several online services for the *Tufts University Diet & Nutrition Letter*. He uncovered a number of claims he said are spurious. In one CompuServe forum, individuals were touting the benefits of an alleged apple suppressant containing an ingredient that Lerner claims is essentially "pond scum that floats on the surface of lakes... and has no use as a weight-loss

or treatment for any disease." CompuServe does police its forums, a spokeswoman says, but becomes aware of a problem, it will launch an investigation.

In another incident, *MMWR* found online bulletin board users stating that vitamins A, C, E, and B12 "have been found to be effective in slowing and even reversing multiple sclerosis." The *Tufts* quotes Dr. Stephen Baran, a health fraud expert, who says the vitamin claim "utterly lacks sense" and notes there is no such thing as vitamin E. The lesson is clear: Whether in cyberspace or the doctor's office, it's wise to seek a second opinion. *Edward*

Medical Advice In Cyberspace

AMERICA ONLINE 800 827-6364. Health & Medical Chat forum has 23 support groups. Cerebral palsy, multiple sclerosis, and mental-illness organizations are represented.

BLACK BAG BBS 610 454-7396.* News and message boards on a variety of medical topics. Features disease and symptoms database. You can also download lists of other health-related boards.

CENTERS FOR DISEASE CONTROL & PREVENTION 404 639-3534. Offers the respected and technical *Morbidity & Mortality Weekly Report* and other CDC publications over the Internet.

COMPUSERVE 800 848-8199. Serves as a gateway to numerous databases including Medline, Rare Disease Database, and National Cancer Institute's Physician Data Query. Many forums.

MEDLINE 800 272-4787. Mammoth database from the National Library of Medicine houses more than 7 million references and abstracts from 4,000 medical journals used by doctors and laypeople.

PRODIGY 800 776-3449. Has primers and other articles under Health Topics section. Also features *Consumer Reports* health-related stories and separate health and medical bulletin boards.

*Modem number

ering a new piece of research or discussing symptoms with others who have a common experience, newly informed patients can go back to their doctors and ask: "Hey, what about this?" Many people who log onto the National Institutes of Health Information Center, explains system operator Dennis Rodrigues, "didn't feel their physician had spent enough time with

with online compatriots: "The thing I like is that [the online environment] gives the patient more control."

By its very nature, cyberspace provides a shroud of privacy for those who don't want to go public with their illnesses. In fact, the doctors who run the HealthSource BBS in Tampa ask questioners who want to remain anonymous to type ANON

One caveat: It may be hard to assess the credibility of online information

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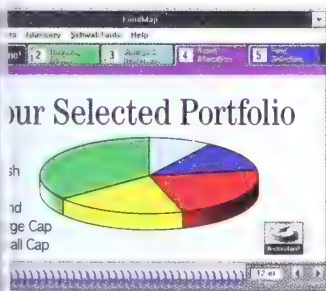
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Once again, certain segments of the financial world are in turmoil. Institutions that once seemed unshakeable, from major corporations to banks to governmental bodies,

have suffered devastating losses caused by speculative investments and derivatives. Poor advice was given to customers and partners. Fad, fashion and speculation were the rulers. Perhaps now we will hear of a return to the basics, and amazingly, the very same

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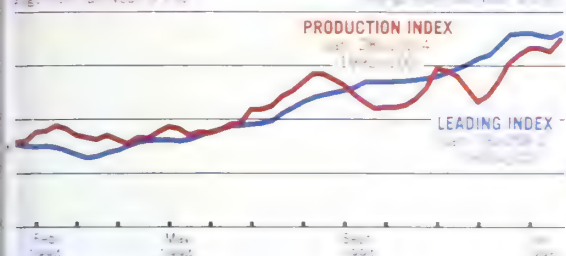
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Business Week Index

PRODUCTION AND LEADING INDEXES

Change from last week: 0.1%
Change from last year: 7.1%



Indexes are 4-week moving averages. The production index rose in the week ended Jan. 28. Seasonally-adjusted electric power, autos, and trucks led the gain. Before calculation of four-week average, the index jumped to 125.3 from 121.9 the week

ending index also increased in the latest week, paced by faster growth in materials prices and the M2 money supply. The unadjusted index rose to 256.9 from 257.5 in the previous week.

Source: Index compiled by MHI. *Historical data available from CIBC

LEADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (2/3) S&P 500	478.16	467.56	+1.4
GOVERNMENT BOND YIELD, Aaa (2/3)	8.33%	8.49%	-20.2
INDUSTRIAL MATERIALS PRICES (2/3)	113.8	114.5	-0.6
BUSINESS FAILURES (1/27)	NA	266	NA
REAL ESTATE LOANS (1/25) billions	\$463.2	\$463.4r	+0.4
M2 MONEY SUPPLY, M2 (1/23) billions	\$3,590.2	\$3,587.6r	+0.7
UNEMPLOYMENT CLAIMS, UNEMPLOYMENT (1/21) thous	325	338r	-10.5

Source: Center for International Business Cycle Research (CIBC), Standard & Moody's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures of companies), Federal Reserve, Labor Dept. CIBC seasonally adjusts data on business failures and real estate loans. *Historical data available from CIBC

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
LIBOR FUNDS (2/7)	5.94%	6.00%	3.20%
COMMERCIAL PAPER (2/7) 3-month	6.14	6.24	3.50
GOVERNMENT SECURITIES OF DEPOSIT (2/8) 3-month	6.15	6.23	3.40
MORTGAGE (2/3) 30-year	9.15	9.32	7.08
FIXED RATE MORTGAGE (2/3) one-year	6.76	6.83	4.20
ADJUSTABLE RATE MORTGAGE (2/8)	9.00	9.00	6.00

Source: Federal Reserve, HSH Associates, Reuters Holdings PLC

Data in the production indicators are seasonally adjusted in computing the BW index. *Estimated and not listed include: 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (2/4) thous. of net tons	2,040	2,001#	+10.2
AUTOS (2/4) units	139,633	140,384#	-7.8
TRUCKS (2/4) units	114,400	115,400#	-1.8
ELECTRIC POWER (2/4) millions of kilowatt-hrs.	61,394	62,932#	-3.9
CRUDE-OIL REFINING (2/4) thous. of bbl./day	13,438	13,404#	+1.8
COAL (1/28) thous. of net tons	21,269#	21,939	+1.1
PAPERBOARD (1/28) thous. of tons	932.8#	907.6r	+6.5
PAPER (1/28) thous. of tons	837.0#	841.0r	+1.6
LUMBER (1/28) millions of ft.	476.6#	479.6	-2.6
RAIL FREIGHT (1/28) billions of ton-miles	24.0#	24.0	+6.2

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., Southern Forest & Paper Association, WWPAA, SFPAA, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (2/8) \$/troy oz.	374.600	376.250	-2.4
STEEL SCRAP (2/7) #1 heavy, \$/ton	144.50	147.00	+3.6
COPPER (2/8) \$/lb.	142.0	146.0	+50.9
ALUMINUM (2/4) \$/lb.	101.5	104.0	+66.9
COTTON (2/4) strict low middling 1-1/16 in., \$/lb.	89.50	89.29	+23.9
OIL (2/7) \$/bbl.	18.43	18.46	+26.2

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (2/8)	98.92	99.46	+0.5
GERMAN MARK (2/8)	1.53	1.52	+0.7
BRITISH POUND (2/8)	1.55	1.58	+1.46
FRENCH FRANC (2/8)	5.30	5.28	+5.96
ITALIAN LIRA (2/8)	1617.0	1609.0	+695.7
CANADIAN DOLLAR (2/8)	1.40	1.41	+1.34
MEXICAN PESO (2/8)	5.325	5.500	+3.20

Sources: Money News, major banks. Currencies expressed in units per \$1.00 unless noted

THE WEEK AHEAD

SALES

Feb. 14, 8:30 a.m. ▶ January sales are expected to show a slim gain, according to the median forecast of economists surveyed by MMS International, of McGraw-Hill Inc., mainly reflecting looking auto sales caused by a lag in Detroit's reporting dates. Nonauto sales could be up a stronger 0.7%.

COMMERCE PRICE INDEX

Feb. 15, 8:30 a.m. ▶ The Jan. will show a 0.2% increase, say the economists, the same as in December. The index, which excludes energy and food, is up 0.2%, after the previous 0.1% rise.

INDUSTRIAL PRODUCTION

Wednesday, Feb. 15, 9:15 a.m. ▶ January industrial output at the nation's factories, utilities, and mines is expected to post a 0.4% increase, says the survey, following December's 1% gain. Capacity utilization will edge up a tenth of a point, to 85.5%, from December's 15-year high.

BUSINESS INVENTORIES

Wednesday, Feb. 15, 10 a.m. ▶ December inventories in manufacturing, wholesaling, and retailing most likely increased by 0.5%, say the forecasters, following November's 0.7% gain. Stock levels have risen sharply in recent months, but overall sales have been sturdy as well.

HOUSING STARTS

Thursday, Feb. 16, 8:30 a.m. ▶ Despite January's unusually mild weather, higher mortgage rates are expected to take a toll on the month's housing starts. The economists look for starts to fall by 4.3%, after December's 1% drop. Sales of new homes are softening, and based on current sales rates, the one-month supply of unsold homes stood near a four-year high in December.

INTERNATIONAL TRADE

Friday, Feb. 17, 8:30 a.m. ▶ The economists project that December's trade deficit for goods and services will narrow slightly to \$10.4 billion, after having widened to \$10.5 billion in November.

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Index to Companies

This index gives the starting page for a story or feature with a significant reference to a company. Most subsidiaries are indexed under their own names. Companies listed only in tables are not included.

A

Abbey Healthcare 86
Advanced Micro Devices 88, 89
A.G. Edwards 70
Albany International 91
Alias Research 44
AlliedSignal 66
Allmerica Securities Fund 78
American Express 40, 92
America Online 101
Ameritech 92
Andersen Consulting 92
Anheuser-Busch 51
Animation Studios 44
Apple Computer 20, 44
Area Code Cafe 92
AT&T 6, 44, 92, 97
Avitas 40

B

Bayerische Hypotheken- und Wechsel-Bank 56
Bell Atlantic 92
BellSouth 92
Ben & Jerry's 51
Berkshire Hathaway 72
BIS Strategic Decisions 92
Blockbuster 48
Boeing 32, 66
Burlington Coat Factory 88

C

Cablevision Industries 37
Call-America 92
Cambridge Human Resources 26
Charles Schwab 110
Chrysler 32, 66, 110
Comcast 92
Commerzbank 56
Compaq Computer 20, 88, 89
CompuServe 101
Continental Cablevision 92
Cooper 72
Coram Healthcare 86
Corbis Publishing 20
Cox Enterprises 92
Creative Artists Agency 92
Cushman & Wakefield 54
Cyrix 88

D

Daimler Benz 56
Davis Polk & Wardwell 68
Dean Witter Reynolds 70
Delta Air Lines 68
Deutsche Bank 56

Deutsche Telekom 56, 92

Dresdner Bank 56

E

Emerson Electric 66
Energis 92
Engex Fund 78
Entergy 92
Enterprises 44

F

Fidelity Investments 16, 70
First Australia Fund 78
Ford 32
Fox 64
FPA New Income Fund 16
Frontier 97

G

GE 17, 66, 70
Genentech 38
General Magic 44, 92
Geoworks 44
GM 48
Goldman Sachs 64
Grand Metropolitan 86
GTE 92

H

Harman International 51
Hauser Communications 92
HCI USA Distribution 8
Heinz (H.J.) 48
Hewlett-Packard 20, 88
Hitachi 64
Homedco Group 86
Honeywell 66
Houston Industries 37
Hussmann 86

I

IBM 20, 36, 48, 89, 92
ICA 54
Inland Steel 51
Intel 88, 89

J

Jackson Grant 70
JB Trucking 89
Johnson & Johnson 8, 38
J.P. Morgan 26

K

Kemper Securities 48, 78
Kidder Peabody 70
KKR Group 86
Klöckner-Humboldt-Deutz 56
Knowledge Adventure 92
KPMG Peat Marwick 92

L

La Salle Partners 54
Latin American Equity Fund 78

LLDS 92

Lebedinsky Mining 60
Lehman Brothers 70, 72, 76
Lipper Analytical Services 16
Litton Industries 66

M

Magma Copper 51
Matsushita 44, 64
MCA 64
McCaw Cellular 91, 92
McGraw-Hill 107
MCI 16, 92
Merrill Lynch 70, 74
MFS Communications 92
MGM/UA 64
Michigan National 48
Microdin 60
Microsoft 20, 32, 44
Midas International 86
MIPS Technologies 88
MMS International 107
Morgan Stanley 92
Morningstar 70, 78
Motorola 44, 51, 91

N

NationsBank 38
NatWest Securities 66
Nestlé 48
Network Dynamics 92
New Germany Fund 78
NexGen 88, 89
Nike 32
Northville Industries 51
Northwest Airlines 66
Nynex 92

O

Olympia & York 54
OPTi 88

P

Pacific American Income Shares Fund 78
Pacific Telesis 92
PaineWebber 70, 75
Pan Am 68
Pepsi-Cola General Bottling 86
Pet 86
Phar-Mor 48
Philips Electronics 36, 64
Pilgrim Group 16
Pilgrim Prime Rate Trust Fund 16
Pioneer 64
Polaroid 48
Price Waterhouse 34
Prodigy 101
Prudential Securities 70, 78
Public Service Electric & Gas 92

Q

Quaker Oats 48

R

Ralston Purina 48
Reichmann International 54
Rochester Telephone 92, 97

Rockwell International 66
Rossisky Credit Bar

S

Saab 48
Salomon 6, 36, 48
Sanford C. Bernstein Saturn 51
SBC Communications
Schine On-Line Services 101
Seagram 37
Siemens 66
Silicon Graphics 4
Smith Barney 70
Software Publishing
Sony 44, 64
Southern New Eng Telecom 92
Southwest Airlines
Spectrum Holobyte
Sprint 92
Starbucks 51
Stoeber Glass 8
Sun Microsystems
Swiss Helvetia Fur

T

Tele-Communications
Thermo Trax 91
Thomson 61, 64
Time Warner 37, 6
97
Toshiba 37, 44, 64
Trans-World Metals
Trinova 86
Trust Company of West/Dean Witter
Convertible Trust
Turner Broadcasting

U

United Airlines 40
USLife Fund 78
U.S. Short-Term U Government Fund
U S West 37, 92

V

Vanguard Group 7
Viacom 92
VocalTec 6
Voipe Welty 86

W

Wal-Mart Stores 4
Walt Disney 64, 9
Warner Home Video
Wavefront Technologies 44
WEFA Group 92
Whitman 86
William Blair 70
Williams 92
Wiltel Communications Systems 92
Wyatt 26

Z

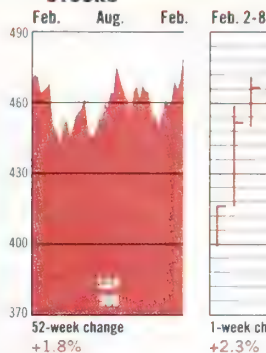
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Investment Figures of the Week

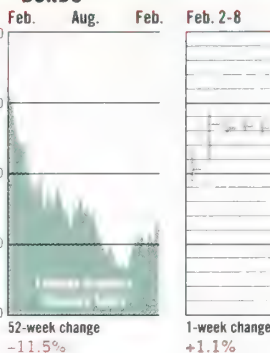
STOCK MARKET

The stock market went on a roller coaster ride on Feb. 3, as investors received a report showing more jobs than expected. Reacting to a report that the unemployment rate fell 0.3 points in January, investors wagered that economic growth was slowing and stocks were at a peak. Bonds and so did blue chips, Dow Jones industrial averaging 58 points, to 3929. The market's recovery to 4000 fizzled in the next days, and the dollar rose due to mixed economic

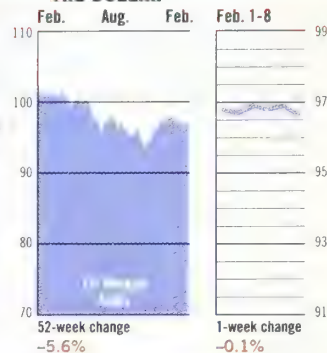
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

INDEXES	Latest	% change	
		Week	52-week
DOW JONES INDUSTRIALS	3935.4	2.3	0.1
COMPANIES (S&P MidCap Index)	177.2	3.2	-2.3
COMPANIES (Russell 2000)	253.8	2.5	-4.3
COMPANIES (Russell 3000)	275.5	2.4	0.7

INTERNATIONAL STOCKS	Latest	% change (local currency)	
		Week	52-week
FINANCIAL TIMES 100	3072.5	1.8	-10.4
NIKKEI INDEX	18,290.3	-2.4	-7.8
TSE COMPOSITE	4104.2	2.1	-8.0

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.89%	6.05%	3.31%
30-YEAR TREASURY BOND YIELD	7.64%	7.74%	6.42%
S&P 500 DIVIDEND YIELD	2.69%	2.75%	2.51%
S&P 500 PRICE/EARNINGS RATIO	16.4	16.1	22.0

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	459.8	459.0	Positive
Stocks above 200-day moving average	47.0%	41.0%	Neutral
Speculative sentiment: Put/call ratio	0.60	0.62	Neutral
Insider sentiment: Vickers sell/buy ratio	0.84	0.87	Positive

BLOOMBERG FINANCIAL MARKETS

STOCK GROUPS

WEEK LEADERS	% change		Strongest stock in group	% change		Price
	4-week	52-week		4-week	52-week	
UTILITIES	13.3	7.7	MCDONALD'S	15.7	12.2	33 1/4
HEALTH CARE SERVICES	12.3	1.9	ALZA	16.2	-11.8	22 3/8
ENTERTAINMENT	12.1	5.4	WALT DISNEY	13.3	15.8	52 1/8
INSURANCE	11.5	-4.6	TORCHMARK	17.0	-15.4	41 1/4
BANKS AND LOANS	10.3	-0.7	GREAT WESTERN FINANCIAL	13.9	4.2	18 1/2

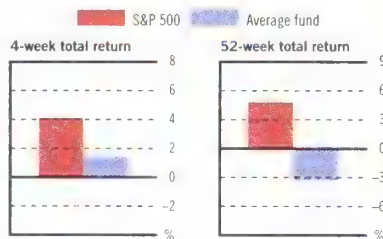
WEEK LAGGARDS	% change		Weakest stock in group	% change		Price
	4-week	52-week		4-week	52-week	
TELEPHONE	-10.5	-31.3	CHRYSLER	-14.3	-26.6	45 1/8
COMPUTERS	-8.4	-13.8	INLAND STEEL INDUSTRIES	-16.4	-15.6	29 7/8
MINING	-8.1	-26.7	ROADWAY SERVICES	-10.7	-27.2	50 1/4
RETAIL	-6.4	-5.3	PHELPS DODGE	-9.9	-0.5	54 5/8
DUTY TRUCKS	-5.9	-23.7	PACCAR	-10.3	-24.9	42 5/8

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MUTUAL FUNDS

FOUR-WEEK TOTAL RETURN	%	LAGGARDS	FOUR-WEEK TOTAL RETURN	%
WRIGHT EQUIFUND-MEXICO NATL. FID. EQTY.	9.8			
BULL & BEAR GOLD INVESTORS	9.3			
JAPAN	9.3			

52-WEEK TOTAL RETURN	%	LAGGARDS	52-WEEK TOTAL RETURN	%
MONITREND GOLD	28.9			
STEADMAN OCEANOGRAPHIC TECHNOLOGY	27.9			
STEADMAN AMERICAN INDUSTRY	27.6			



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RELATIVE PORTFOLIOS

Relative portfolios represent the performance of a \$10,000 investment one year ago.

Percentages indicate total returns.

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\$10,504
+2.21%

Money market fund
\$10,495
+0.26%

Foreign stocks
\$10,468
+0.43%

Gold
\$9,808
-0.11%

Treasury bonds
\$9,119
+0.90%

Data on this page are as of market close Wednesday, Feb. 8, 1995, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as

of market close Feb. 7. Mutual fund returns are as of Feb. 3. Relative portfolios are valued as of Feb. 7. A more detailed explanation of this page is available on request. r=revised

DON'T LET CHINA OFF THE HOOK

First Japan, now China? After an impressive, nuanced show of force in placing \$1 billion of punitive tariffs on Chinese exports to combat the flagrant piracy of U.S. products, the Clinton Administration is in danger of signing a deal that does little to shrink America's growing \$30 billion deficit with China. That would be a big mistake.

Throughout the cold war, the U.S. accepted Japanese protectionism because of overriding geopolitical concerns. Lost exports, slower growth, and fewer American jobs were the price of Tokyo's continued political support in the fight against communism. Besides, the bulk of the global trading system was open, and the U.S. could compete successfully in Europe and other markets where the playing field was more level.

We now see that the price of solidarity was too high and that Japanese-style mercantilism is no harmless economic anomaly. That is why Washington—and Corporate America—should think twice about the specter of Chinese mercantilism. If China can create a closed economy that feeds off never-ending trade surpluses with the U.S., the free-trade system could break down. It's not only China's size—its economy is expected to rival that of the U.S. in three decades—but its role as a model for the rest of Asia that matters. The U.S. would be hard put to remain true to its free-trade principles if all of Asia goes mercantilist.

To a growing number of Americans, the benefits of free trade are already elusive. Traditional opposition from unions on the left is being joined by new opposition on the right, from freshman Republicans to European businessman Sir James Goldsmith. The bipartisan support behind the U.S. role in financing the expansion of free markets and democracy around the world that began with the Marshall Plan is eroding. Increasingly, the forces of protectionism and interna-

tionalism do battle in Congress. Neither the Democratic Republican leadership, for example, could deliver the vote to provide loan guarantees to help Mexico. And the 1990 American Free Trade Agreement and the General Agreement on Tariffs & Trade passed with the slimmest of margins.

It may be that Beijing's leadership crisis makes it hard for China to accommodate the U.S. But the confusion surrounding the imminent passing of Deng Xiaoping is also an opportunity. China is not only undergoing a succession crisis, it is deciding what kind of capitalism it wants—closed or open, state-owned or private, inward-looking or internationalist. Does it enforce its laws on intellectual-property rights, or does it not?

Now is a perfect time for Washington to make it clear to the U.S. and the global trading system are open only to those who play by the rules. Running 29 factories that counterfeit American software and video disks is simply not acceptable in a trading partner. It is more than a matter of knocking off copies of *The Lion King*. The intellectual-property conflict revolves around Chinese piracy of U.S. technology and management knowhow on a broad scale. After General Corp. invested millions of dollars in China to build a plant, it discovered to its horror that the Chinese were knocking them off—with no apology (page 32).

This is a critical moment for free trade. U.S. Trade Representative Mickey Kantor should make it plain that the trade imbalance must end and the trade imbalance must be shrunk before the U.S. allows China to join the new World Trade Organization. China and the U.S. can prosper together only if they can reap benefits from being in each other's markets. That message should be delivered to Beijing by Kantor—and all of China's trading partners, for that matter. Anything less will undermine free trade around the globe.

BROKERS SHOULD HEED THE WAKE-UP CALL

Have you looked at your brokerage statement lately? What's most noticeable is what isn't there. Among the missing: a tally of total commissions paid and the rate of return for stocks and bonds in the account for the quarter or the year.

In fact, woefully inadequate statements are symptomatic of an industry that has apparently wanted to keep investors in the dark. Until recently, Wall Street's dirty little secret was a compensation system that sometimes puts brokers' interests in conflict with customers'. Among the most questionable practices: paying brokers extra commissions for selling firm-sponsored mutual funds and life insurance; pitching a "product of the month" to clients; and compensation schemes that provide tremendous incentives for "churning" (page 70).

Thankfully, some of the worst practices are being eliminated. The long-overdue changes result largely from a reform-minded crusade by Securities & Exchange Commission Chair-

man Arthur Levitt Jr., a former brokerage firm executive and head of the American Stock Exchange. At his urging, the biggest Wall Street brokerage firms have cooperated in a soon-to-be-released task force study that will recommend sweeping changes to end egregious practices.

The stakes for Wall Street's traditional, big-name brokers are high. If brokers lose much more public confidence, the billions of dollars will flow faster into the hands of mutual funds, independent investment advisers, and discount outfits such as Charles Schwab & Co. A failure by the industry to become more investor-friendly also would likely bring pressure from regulators. Levitt is not a proponent of new regulations; he believes the heavily controlled industry doesn't need more rules. The SEC could require firms to disclose to customers details of commissions and performance. Come to think of it, investors should start demanding these changes right away.

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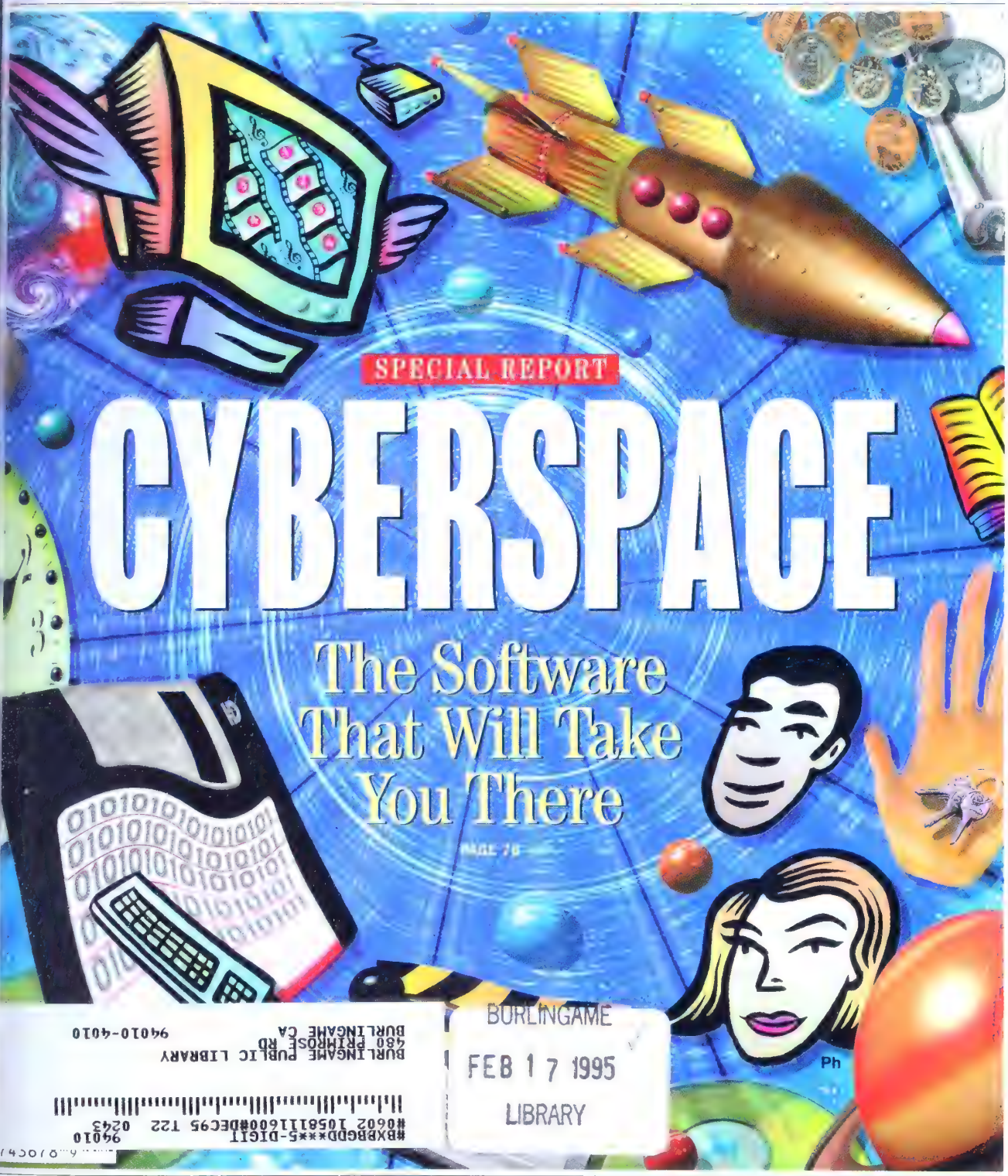
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55 WEEK
February 27

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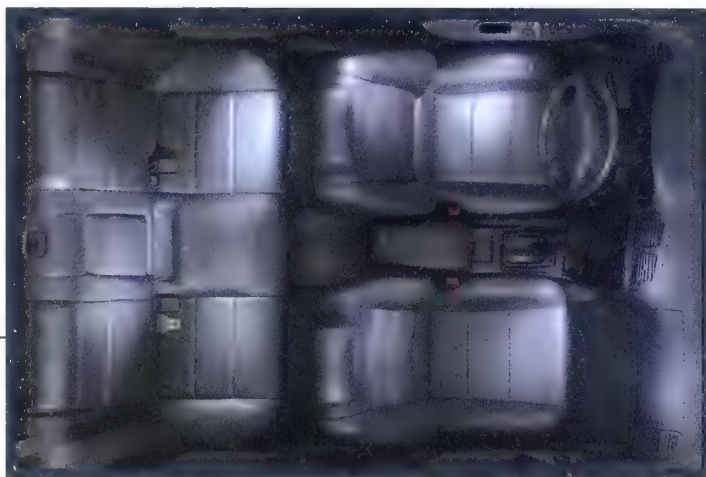
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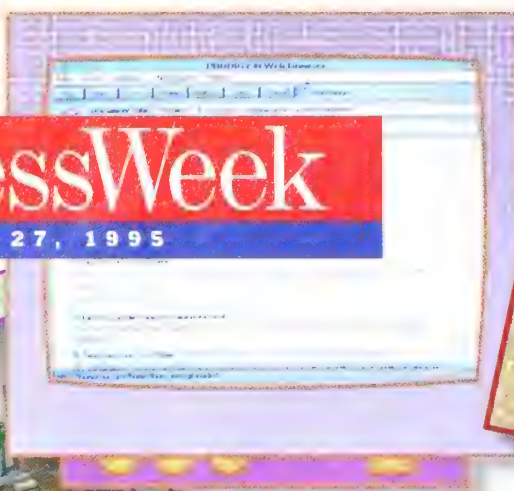
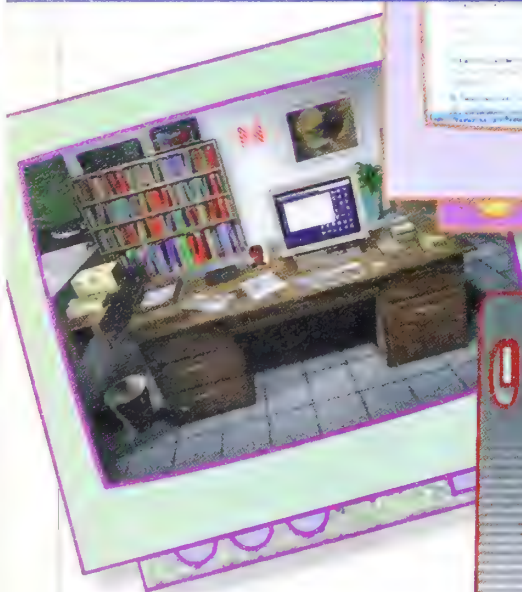
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FEBRUARY 27, 1995



SPECIAL REPORT

CYBERSPACE

Software makers rushing to cash in with powerful new programs for a virtual electronic marketplace page 2

Special Report

78 SOFTWARE'S NEW WORLD ORDER

A great cyberspace race is under way, and programs that can create a business-friendly environment and securely manage online transactions will come out on top

80 THE COLOR OF CYBERMONEY

Creating the coin of the digital realm

86 SAFE BUSINESS ON THE NET

RSA's encryption system holds the key

News: Analysis & Commentary

38 MICROSOFT: THE DEAL IS OFF

Judge Sporkin's rejection of Justice's antitrust agreement with Microsoft has rivals gleeful—but for how long?

40 PUBLIC ENEMY NO. 1 AT MICROSOFT

Meet Gary Reback, the lawyer who helped undo the consent decree

41 SENATOR DANGERFIELD?

Why Larry Pressler may be in over his head in the telecom wars

42 BYE-BYE, TAX CUTS?

The GOP is backing off many of the lavish breaks proposed in the Contract With America

43 PROFITS: WOW!

They were up a colossal 42% on average on a sales hike of just 10%

44 COMMENTARY

It's time for politicians to give Medicare a dose of managed care

46 UP FROM THE CEREAL AISLE

Ralph Burkle is building up a multibillion-dollar supermarket empire

47 THIS IS WHAT THE FCC HAD IN MIND

Its tax break worked well with black broadcaster Don Cornwell

48 AN EYE-POPPING MARKUP

Contact-lens wearers can pay up to 24 times as much for small bottles as large

48 DISNEY GOES TO COURT—IN CHINA

U.S. companies are testing the strength of its copyright-infringement laws

50 THIS COMPANY CAN PUT OUT A FIRE

Carpetmaker Milliken kept itself—and a town—going after a key plant burned

51 IN BUSINESS THIS WEEK

International Business

56 FRANCE

A slew of scandals could finally imperil the style of France Inc.

58 MEXICO

Cemex' global reach and cost-cutting are helping it weather the peso

62 MEXICO

The leadership vacuum is getting

66 CANADA

Here, at least, NAFTA is a smashing success: cross-border trade and growth

73 INTERNATIONAL OUTLOOK

Republican favors could hurt T

Economic Analysis

32 ECONOMIC VIEWPOINT

Roberts: It's time to privatize Social Security

34 ECONOMIC TRENDS

Baby boomers' nest eggs, why they save, pay for U.S. managers' labor, final tab on the S&L bailout

35 BUSINESS OUTLOOK

Structural shifts in the U.S. economy have made price pressures less

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LOOKING SOLID

Even as Mexico sinks, cement maker Cemex is thriving, thanks to a program of global diversification

page 58

DAY FOR BILL GATES

Microsoft's deal with Justice Dept. shot down. What's next? page 38



PAPER TRAIL

New evidence links Ron Brown to attempts to land controversial oil deals while he was at the DNC

page 88



BANK BLOODBATH

Hundreds of thousands of bank employees are likely to get axed over the next few years page 98

Government

WASHINGTON OUTLOOK

Unsinkable Alan Greenspan?

BROWN'S WOES GET WORSE

Pres. Clinton outline controversial oil deals

Marketing

WITH WINDOWS AND WALLS

Drift of new stores, plugging brands is the first order of business

Corporation

FLYING HIGH

Alliance with Northwest has turned Delta to a model global airline

IT IS TONING DOWN THE GLITZ

Disenchanted hotelier retools a cost-conscious decade

HE TURNS OVER A NEW LEAF

Former CEO Jack Reilly, the sick conglomerate is getting smaller

Finance

MARKS: PINK SLIPS AHEAD

Employment could plunge as a result of market petition and falling demand

100 WAILING WALL STREET

The bond-market blast of '94 keeps claiming new victims

101 UP ON DOWN MARKETS

Brandes Partners shops abroad

102 JAPANESE ROLLER COASTER

In the wake of the quake, the Nikkei could be in for more battering

104 INSIDE WALL STREET

Sallie Mae and World Corp
A cable operator works the phones
The upside of Upjohn

135 INVESTMENT FIGURES OF THE WEEK

Science & Technology

107 DEVELOPMENTS TO WATCH

Ink capsules, lenses for humongous holograms, changing markers to improve cancer tests, innovations

110 "GADFLY BOB" IN THE CATBIRD SEAT

House Science Committee Chairman
Bob Walker's ideas could become policy

Sports Business

114 LET THE HYPE BEGIN

Sponsors of the 1996 Olympics have to move fast—and watch their backs

Environment

119 GLOBAL WARMING'S HEATED DEBATE

Some nations want tougher limits on carbon dioxide—despite scanty data

Social Issues

120 RETHINKING AFFIRMATIVE ACTION

To survive, it may have to adapt for the '90s

Personal Business

126 INVESTING: Reaching out to women

CASH CARDS: A new kind of plastic

SMART MONEY: Flexible bond funds

POTABLES: Toasting the "Cal-Italians"

Features

6 UP FRONT

14 READERS REPORT

18 CORRECTIONS & CLARIFICATIONS

21 BOOKS

28 TECHNOLOGY & YOU

133 BUSINESS WEEK INDEX

134 INDEX TO COMPANIES

136 EDITORIALS

How not to reform welfare

Put the peso on a tighter leash

Up Front

EDITED BY LARRY LIGHT, WITH RUTH COXETER

I-WAY PATROL

THE GOP'S STUMBLE IN CYBERSPACE

CYBERDEMOCRACY SEEMS TO have backfired on House Republicans, who are big boosters. Speaker Newt Gingrich (R-Ga.) wants Capitol Hill more wired into the Internet, so citizens have direct access to their government. Fine, except for a furious electronic lobbying battle over public access to a Justice Dept. database on court decisions.

The Republicans were stymied on their bid to aid West Publishing, the company that helped set up the database for Justice and also makes a

lucrative living supplying legal citations to private lawyers. West worries that, since the database is part of a public agency, it could be released to Internet bulletin boards—destroying the company's main business. Result:



LAW DATA: Fodder for the Net?

WILD BLUE YONDER

AN AUSSIE INVASION AT ALITALIA

ALITALIA PASSENGERS NOW might hear "G'day" rather than "Buon giorno" from the flight crew. To the vexation of the Italian carrier's unions, Australia's Ansett Worldwide Aviation Services is supplying two planes and their crews as part of Alitalia's turnaround effort. Ansett, owned by media magnate and union scourge Rupert Murdoch, delivers operating costs that are at least 35% lower than on Alitalia's fleet.

Angry at what they see as a brazen bid to circumvent costly union contracts, pilots and crews struck the airline Feb. 13 and 14, and it canceled one-third of its flights. They returned to the bargaining table Feb. 15.

But no-nonsense CEO Roberto Schisano says he is bent on cutting costs at Alitalia, which lost \$172 million last year. The problem is low productivity. Alitalia pilots earn around the \$100,000-per-year European norm, but work far less than most. Schisano has rejected a union

plan to hike pay in return for more hours in the air, saying previous such deals failed. He has to hope that the Italian government, Alitalia's main

TALK SHOW "We must choose between pulling ourselves into the late 20th century or remaining mired in the tired and abandoned policies of the Great Society."

—New York Mayor Rudolph Giuliani, on his drastic budget cuts

Chairman William Clinger (R-Pa.) recently tried to push a measure through his House Government Reform & Oversight Committee aimed at blocking public access to the database without West's O.K. McGraw-Hill, publisher of **BUSINESS WEEK**, backed West.

Outraged, Naderite lobbyist Jamie Love, head of the Taxpayer Assets Project, posted a note on the Net that decried the provision as thwarting access to public documents.

Lawmakers were flooded with fax and E-mail protests. The committee overwhelmingly voted down Clinger's proposal, and it now says it plans to give the idea more study. *Catherine Yang*



CAREY: A dose of tough lo

UNION DUES

BROTHERHOOD VS. BROTHER

THE TEAMSTERS' NEW REFORM leadership is ratcheting up drive against corruption, using the same antiracketeering laws the feds did to crack down on the union in the late 1980s. Led by reformer Ron Carey, the International Brotherhood just filed a federal civil suit charging the former officials of Chicago-based Local 705, its attorney, and doctor bilked the local out of \$4 million. The Racketeer-Influenced & Corrupt Organizations (RICO) laws provide for treble damages.

The suit accuses former Local 705 President Daniel Liguoritis—ousted from the union in 1992—of channeling money from pension and health funds to cronies. Example: nearly \$2 million to finance an upscale restaurant in downscale Teamster City, where it lasted seven months. The suit says the owner, Angelo Kokas, was a convicted felon with mob ties.

The union charges Liguoritis with soliciting a \$25,000 bribe from Lucchese crime family associates. Plus, the local's doctor, William Dalesandro, allegedly directed patients to clinics he had stake in and billed the union for services not performed. The suit says attorney Sherman Carmell aided and abetted these activities. None of those named could be reached for comment. *Kevin Kelly*

shareholder, won't cave in to union demands.

The pressure is especially intense because Europe's flag-carrier airlines face a U.S.-style deregulation in 1997. Then, low-cost upstarts can begin taking traffic away from them. *John Rossant*

THE LIST CORNER-OFFICE LEGAL AID

Bill still has friends in these Republican times, even in the executive suite. And he needs them: The tab for the President's legal defense against Whitewater allegations and Paula Jones' harassment charges stands at \$1.2 mil-



lion. Hence, the creation of the Presidential Legal Expense Trust, which has raised \$608,080. More than 5,200 folks have chipped in, from baby-sitters to Hollywood's Barbra Streisand. And a number of CEOs at the \$1,000 max.

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Up Front

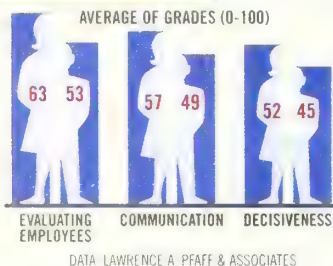
WORKPLACE SURVEY

A WOMAN'S PLACE? IN CHARGE

WOMEN ARE BETTER BOSSES. That's the verdict from a survey of more than 9,000 managers who graded male and female superiors on 20 skills ranging from communicating to decisiveness. According to

EMPLOYEES RATE BOSSES BY GENDER

How they do at:



Lawrence A. Pfaff & Associates, the Kalamazoo (Mich.) consulting firm that did the study, women are rated the best in every category.

The gap is the biggest on planning, making changes,

and evaluating employee performance, where females outshine males by 10 points. Ratings are like school grades, from 0 to 100. So, for example, women score 56 on planning, vs. 46 for men. The sexes come the closest on delegating authority, 55-54.

Why would women make better chiefs than men? Says Larry Pfaff, the firm's president: "Women are still brought up to be more social. Those skills pay off in the workplace."

This survey certainly seems to dispute old notions that "male" qualities make for better leaders. But other surveys indicate no real differences exist between genders. Jeffrey Sonnenfeld, director of Emory University's

Center for Leadership and Career Studies, says these studies show a greater gap between individuals than between sexes. He decries "creating a cartoon character of gender differences." □

PUDGEBALL NATION

SEATTLE IS ON A (CINNAMON) ROLL

FIRST COFFEE BARS, NOW bun shops. As it did with Starbucks, Seattle has launched another trendy chain, this one selling cinnamon buns. Like Starbucks, Cinnabon shops are popping up in cities across the land. Cinnabon sells huge, nine-ounce cinnamon rolls fresh from the oven, rich and sticky, dripping with margarine and spiced with Indonesian Korintji cinnamon. So what if a bun costs \$1.89 and has 810 calories (a Minibon goes for \$1.39, with 330 calories)? Long lines form outside Cinnabon shops.

Started in 1986, \$100 mil-

lion Cinnabon has averaged 25% annual sales growth. It now has 276 shops (about half franchised) in 37 states, Canada, and Mexico, with a 500-store goal by 2000. Its parent, Restaurants Unlimited,

hopes to go public within three years.

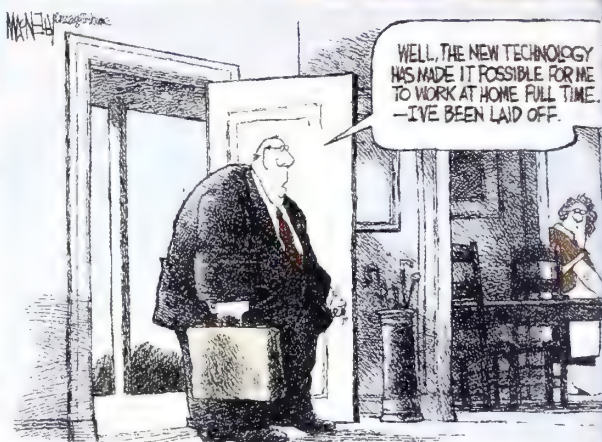
The company calls its shops "bakeries" because customers can breathlessly watch the rolls being

made. They come, says President Dennis Waldron, "for the emotional experience.... It's not a fuel stop." Oh, yes. Cinnabon also sells custom-blended coffee, called Ruby-moon. After all, it's from Seattle. *Dori Jones Yang*

BEHOLD: The \$1.89 bun



DRAWN & QUARTERED



FRENCH CONNECTION

ONE MAN'S STEED IS ANOTHER'S SUPPER

HOSS RUSTLING HAS BECOME a nagging problem lately. In Texas, everything from the old gray mare to champion quarter horses are disappearing from barns and pastures. "We're up to one horse missing per day now," says Kathy Fleming of the Texas Horse Owner's Assn. A few years back, it was two or three horses per week. Now, around Houston, it's so bad authorities are holding low-cost "branding days" to mark horses.

Blame most of it on a longstanding appetite for horse meat in France and Belgium. The number of horse butchers has declined there in recent decades as tastes turned

to other fare. Too much. The continued demand *cheval* can't be met domestically. Stolen horses usually end up in U.S. pack plants, then the meat shipped off to Europe. Packers pay rustlers 75¢ per pound. Since the average horse weighs 1,200 pounds,



DARN! Where's Old Paint?

says Houston Police Officer Cyndi Hogg, "you're talking pretty good money." Compared to an auto, "horses are easier to steal." A whinnies a lot quieter than a squealing car alarm. *Kate Mur*

THE BIG PICTURE

GENERICIS RULE

Increasingly, you can get a low-cost generic drug instead of a brand name. With more categories of pharmaceuticals open to generics, drug-price inflation slowed to 3.3% last year from 9.9% in 1990.

Brand names must keep prices down to compete.

One impetus for the change: Managed-care providers, eager to reduce expenses, are pushing generic substitution.



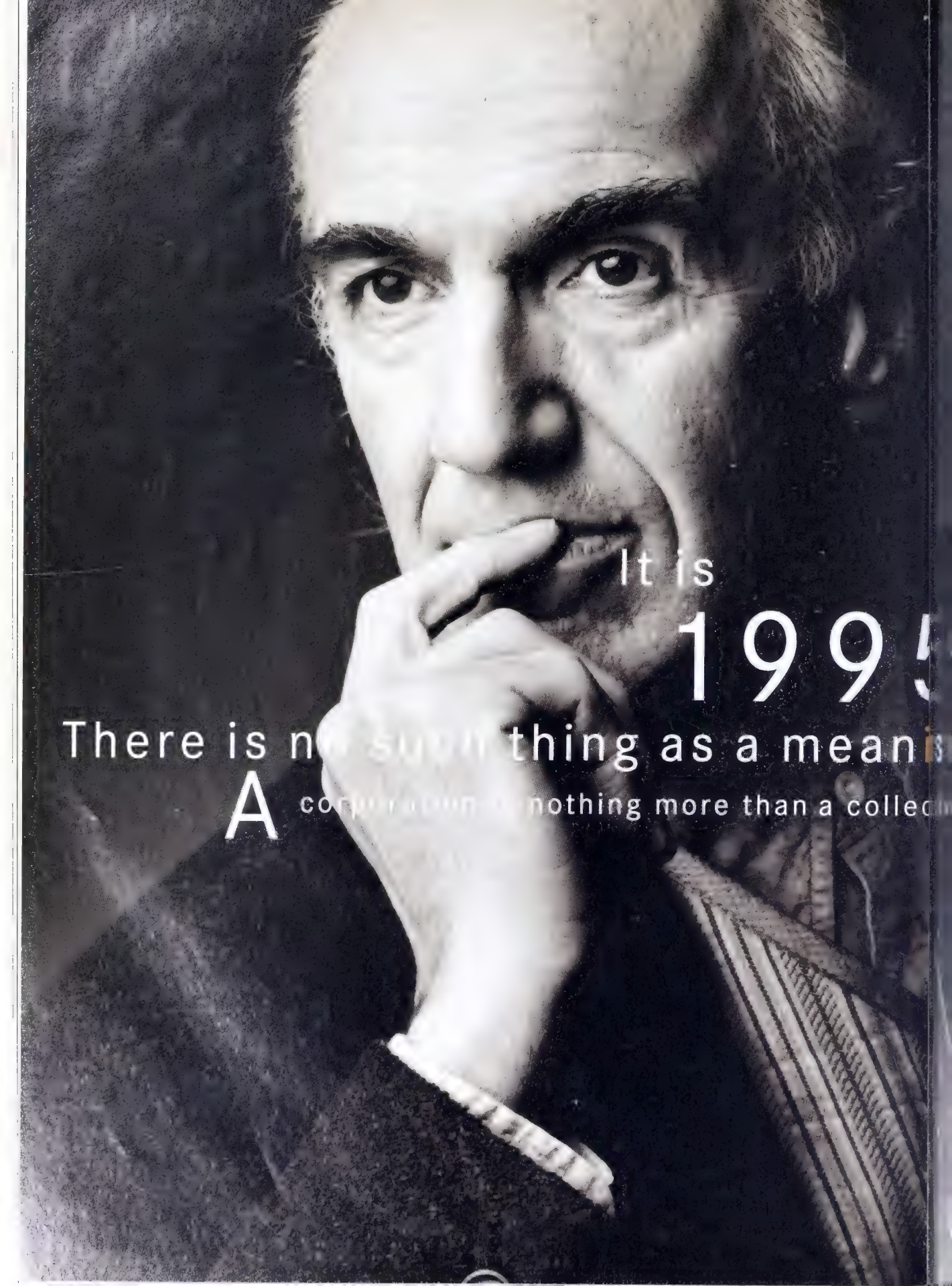


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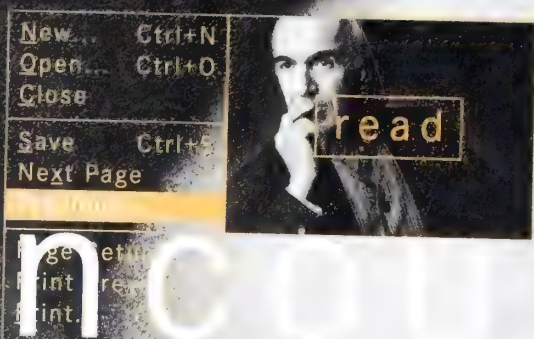
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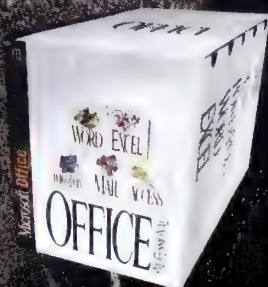
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BEST MUTUAL FUNDS FOR WHOM?

"The best mutual funds" (Cover Story, Feb. 6) states that the best funds were not the ones with the biggest total returns but the ones that gave the best "risk-adjusted" performance. For investors with long time horizons (for example, college funding for young children or long-term retirement planning), volatility is irrelevant. Consciously accepting lower returns than could otherwise be achieved just to have less volatility will virtually guarantee less money at the time when it will be needed.

The best way to evaluate any long-range investment program is by total return. Only when a substantial withdrawal is contemplated over the near term should long-term investments be shifted to lower-returning vehicles to avoid the risk of being forced to cash out at an inopportune moment. The most serious problem in most Individual Retirement Accounts and 401(k)-type accounts is keeping long-term money in inappropriate (read: lower to-

tal return) investments such as money funds and bond funds.

Paul M. P.
 Senior Vice-President
 Wheat First Butcher Shop
 Chadds Ford, Pa.

SANITY, MADNESS, AND THE BUDGET

Your recent comment on fiscal policy—"The GOP's brutal bottom line" (Government, Feb. 6), once again refuses to recognize that the only conceivable, sensible, rational, and politically acceptable road to a balanced budget is paved with deep and immediate cuts in defense and intelligence budgets. The GOP can provide the voters no rationale based on national security concerns for holding defense spending at projected levels much less a proposal for increase.

Tom Murr
 San Jose, Calif.

Your excellent story nicely portrays the kinds of program cuts required to balance the budget per the Contract With America. Thank you for address-

THE MAN WHO MADE ECONOMICS UNDERSTANDABLE

It has been more than 25 years since Leonard Silk wrote for BUSINESS WEEK. But he left a lasting legacy. In the 15 years he was on the staff, from 1954 to 1969, he pioneered a new form of journalism: the coverage of economics as news and public policy.

With the guidance and support of Elliott V. Bell, then editor and publisher, Silk created BUSINESS WEEK's economics department and turned out a

stream of coverage that made the great economics issues of the time understandable to any reader, particularly during the "new economics" era of the Kennedy and Johnson years. BUSINESS

WEEK has consistently built on that tradition to this day.

Leonard, who had a PhD in economics, was also a mentor to many young people. He was generous with his time, sharing ideas and pushing us to make complex ideas accessible to the public.

Leonard Silk died on Feb. 27 at 76. Until his retirement two years ago, his was a familiar name on the pages of

The New York Times, which he joined shortly after leaving BUSINESS WEEK. He will be remembered for his role in leading the transformation of the "dismal science" into the stuff of good reading



LEONARD SILK

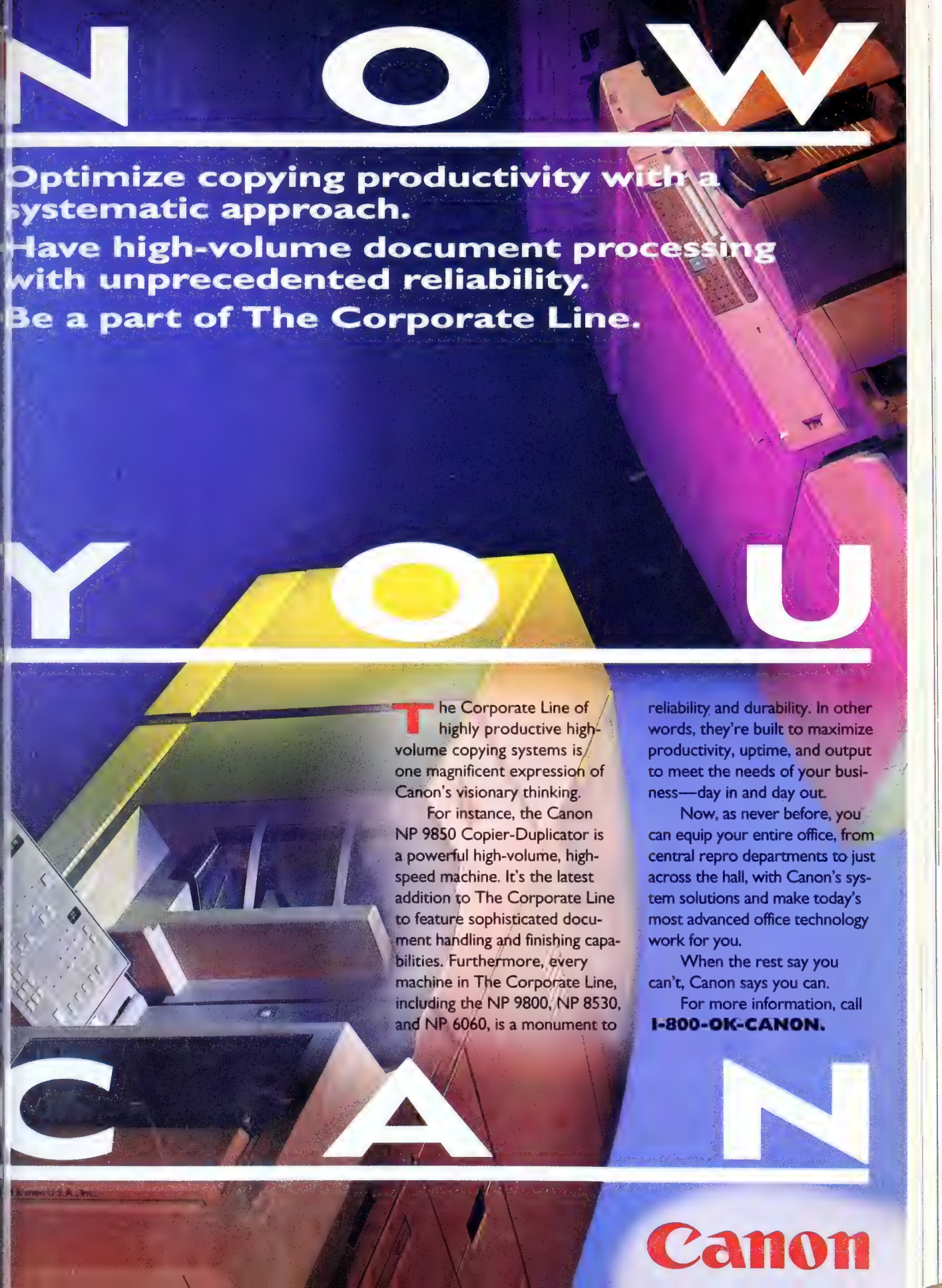
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There is a popular notion (albeit misconceived) that a sports car must, by definition, contain a manual stick shift and clutch pedal.

That only the deft coordination of left foot and right hand can land you in the presence of that divinity who presides over the open road.

That anyone who would think of merely shifting into the "D" position and letting the car do the work must somehow be deprived, never having known the true joy of driving.

Needless to say, we'd like to suggest otherwise. And our reason for doing so is the new M3 Automatic. Stablemate to the car Automobile magazine honored with its 1995 Automobile of the Year award.

Indeed, there was no shortage of accolades for last year's M3. It made Car and Driver's 1995 Ten Best list and Motor Trend's ranking of the Top Ten Fun Cars.

The rest of the automotive establishment was just as complimentary. AutoWeek wrote, "Everyone who drives an M3 wants one in his or her own garage." EuroSport Car said, "This car would be an absolute joy to drive on a daily basis."

And here, perhaps, is one of the many pleasures of owning an automobile like the BMW M3. It is truly a car for driving every day. Whether equipped with the manual transmission Car and Driver called "effortless," or the optional 5-speed automatic.

A gear box specifically engineered to suit the high performance character of the M3, our automatic was designed to give you the feel of a manual. Shifting is crisp and immediate, without the lag you'd normally expect in such a transmission.

A simple tap of your foot on the accelerator is all that's required to experience the eager response and exhilarating quickness that have already made the M3 a legend in the automotive world.

Which brings us to its brilliant 240-horsepower, six-cylinder, DOHC power plant. Specially tuned by our Motorsport Division engineers to match ideally with the new automatic transmission, it delivers high torque at the low end, for strong pick-up at slower speeds.

An abundance of power at the high end means you can accelerate from zero to sixty miles per hour in a mere 6.9 ticks on the clock.

Equally impressive, the M3's massive, ventilated ABS brakes can have you back to zero in just under three seconds.

A firm sports suspension, variable-assist power steering and low-profile 17-inch wheels join forces with our engine/transmission package, providing a direct feel for the road like only a BMW can.

And lest you imagine all this performance arrives at the expense of comfort, be advised that the M3's interior is well appointed with amenities. A micro-filter ventilation system, powerful stereo and multi-adjusting sport seats are all standard.

The result, to put it briefly, is a driving experience you'll be hard pressed to forget.

Call 1-800-334-4BMW to learn more about the new M3 Automatic. A sports car engineered not just to move you quickly, but to move you deeply.

THE ULTIMATE DRIVING MACHINE.



Readers Report

CORRECTIONS & CLARIFICATIONS

"This Mac really does Windows" (Technology & You, Feb. 13) should have identified Reply Corp. in San Jose, Calif., as the company that sells boards enabling Macintosh computers to run Windows software. All the table should have given the list price of a PowerMac 6100 dos Compatible Computer, without keyboard or monitor, as \$2,799.

The item "Robert Haft circles Phar-Mor" (Business This Week, Feb. 20) erred in reporting that Haft had collected a \$34.1 million jury award. A jury awarded Haft the sum, but the decision is being appealed.

what eludes the politicians: Both tax cuts and budget balancing are more rhetorical than real. Yet you don't mention the cost of financing the national debt. I'd like to see a similar accounting of what programs and services we'll forgo in 2002 without tax cuts and given the current trend in deficit reduction.

Bill Marshall
Somerville, N.J.
Starch@aol.com

Your article ends with one House Republican's solution: "I'm going to vote for the amendment. And then I'm going to pray to God that the states don't ratify it." I wish our congressmen would get on with the work they were elected to do: Reduce the deficit, reform welfare, reform health care, and set tax limits. We are sick and tired of more of the same rhetoric and dishonesty. Stop talking and start doing the difficult tasks you were elected to do.

Freida Shattuck
Baltimore

CLINTON'S NEW COVENANT? THANKS, BUT NO THANKS

In "The crux for Clinton: follow through" (News: Commentary & Analysis, Feb. 6), you seem to think the New Covenant is a reasonable vision of government. You quote from Clinton's State of the Union speech: "We should rely on government as a partner to help us do more for ourselves." As a middle-class American who voted for the GOP last November, I see nothing reasonable about that. This government "partner," with my other "partner," the state of Michigan, already takes 40% of my income.

Please, no more partners! We can do more for ourselves if the government gets out of our lives, leaves us alone, reduces its size, and takes less of our

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Currently, 3.4 workers are contributing to Social Security for each retiree collecting benefits. When today's 30-year-olds retire, there will be less than two workers per beneficiary!

Social Security alone may not provide you with the standard of living to which you're accustomed.

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new ways that may help you adjust your strategy to better prepare for the future. Plus, you'll discover the many benefits of adding an IRA to your retirement plan.

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Readers Report

money. So let's get on with it, GOP have two years. Let's slash, let's burn!

Peter Chan
Muskegon, MI

THE GIFT OF SOUND TECHNOLOGY

"They're bearing the gift of sound technology" (People, Feb. 6) shows that device the disabled don't have to be prohibitively expensive. It also shows how corporations working with special technology developers can, with minimum cost impact, broaden the market and help ensure the success of the device.

There was one misstatement of fact in the article when it stated that the Americans with Disabilities Act (ADA) requires employers to hire a certain number of disabled workers. ADA does not establish quotas. ADA only states that an employer cannot discriminate against an otherwise qualified individual based on that person's disability.

Herbert
Goleta, CA

TAXES AS EASY AS ONE, TWO, THREE

Your list of proposals for simplifying income taxes ("So many tax-cutters, little room to maneuver," News: Analysis & Commentary, Jan. 30) reminded me of one that a friend and I drafted in the '30s, while we were at law school. We proposed a tax so simple there would be only three lines on the tax form:

1. How much did you make last year?
2. How much do you have left?
3. Send it in!

Gerald P. Roswell

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BARDIERS

By Bronson
om House • 319pp • \$22

NEST OF VIPERS

By Linda Davies
Doubleday • 406pp • \$23

FREE TO TRADE

By Michael Ridpath
HarperCollins • 346pp • \$23

ATIRE ON THE STREET, USPENSE IN THE CITY

It was a filthy profession, but the money was addicting, and one addiction led to another, and were all going to hell." With that opening sentence, former CS Boston trader Po Bronson launches *Bombardiers*, a send-up of life on bond-trading floor that starts out and never lets up. Bronson's book—aps the most entertaining depiction need and dishonesty on Wall Street to see print—is the best of three

novels by financial world insiders. Others are thrillers: *Nest of Vipers* by Linda Davies, a merchant banker, and *Free to Trade* by onetime manager Michael Ridpath.

Bronson's "bombardiers" are the 37 salespeople in San Francisco of an investment bank, Atlantic Pacific Corp., who "sell" customers with bonds that blow up their portfolios. Sid Geeder, "near-40," is one of the grizzled veterans. Then by hatred for the business, he sells savings and loan bailout bonds, surviving S&Ls, figuring the bonds, losers, will force even more S&Ls to

But that's Bronson's point: Government will just launch another bailout, giving the salespeople a chance to sell the bonds and plant the seeds of the collapse.

Bronson is a major talent, able to write the kind of passages you reread to revel in prose with a compelling cadence all its own: "The corruption language and the manipulation of numbers and the distortion of numbers were part of the art of selling. The salespeople created illusions, and in the prophetic visions of prophecy and gran-

deur, just like any other artists. It was a slippery business, a slimy profession, and the degree of sliminess itself was a slippery slope: little white lies; minor, benign additions; a prick of guilt; slight exaggerations; short-term debt."

Of course, he's working with rich material. Wall Street traders and salespeople are colorful and comical in real life, as Michael Lewis established in *Liar's Poker*, his 1989 memoir of his short career at Salomon Brothers Inc. In fact,

the "pesky salesman," to the dismay of the office chief, who's counting on Igino to sell lots of those bonds. "Well, we have to fire somebody," the Director of Surveillance reasons. "We can't let this happen without some sort of scapegoat."

Instead, the crafty execs turn the crisis into a marketing gambit. They promote Igino to senior vice-president for "finding" the extra collateral, lower the interest rate on the bonds to reflect their enhanced credit quality, and plant

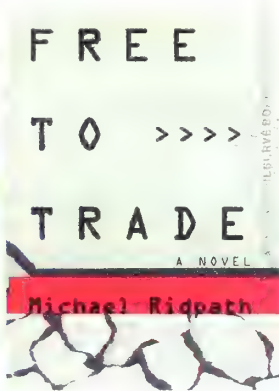
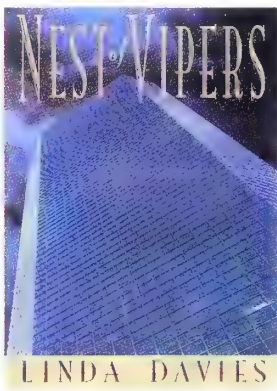
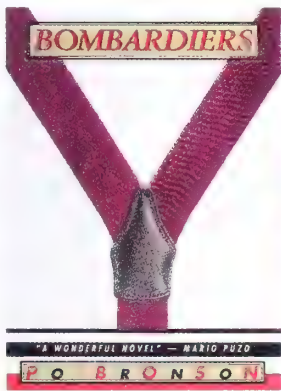
a story in *The Wall Street Journal* about the idealistic young man cutting the cost of rebuilding Eastern Europe.

Such lies don't faze the bosses, but they gnaw at the sales folks, who develop addictions, neuroses, and psychosomatic illnesses. They realize they have to make their

money quickly—before the guilt kills them. Igino doesn't even wait. He vanishes on the eve of the firm's biggest deal—a bond issue to finance a leveraged buyout of the Dominican Republic.

As a setting for fiction, the financial markets offer high drama as well as low comedy, since fortunes and reputations are always on the line. Bronson exploits some of that. There's an effective cliffhanger, for example, in which a salesman-turned-client, angry because he wasn't paid all he was owed when he quit, exacts his revenge—at a cost far greater than four months' commissions. Bronson's main achievement, though, is to keep his readers laughing.

In *Nest of Vipers*, Linda Davies tries to capture the markets' drama. And her book, though less ambitious and less memorable than *Bombardiers*, succeeds as a financial thriller. Set in the City of



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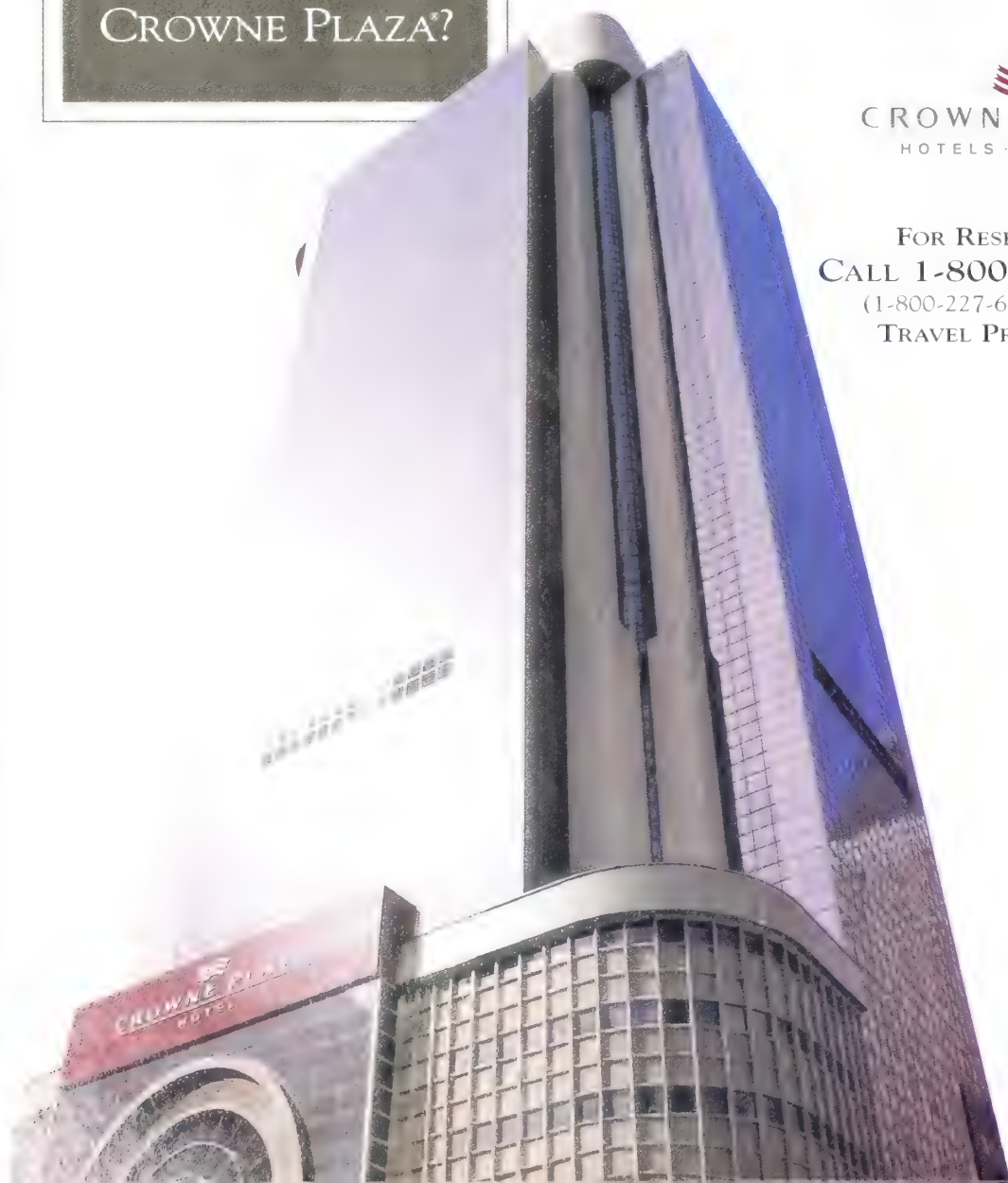
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Books

London, it features currency trader Sarah Jensen—brilliant, beautiful, and rich. She's recruited by the governor of the Bank of England to find out why the foreign exchange desk at a certain bank scores big whenever G-7 finance ministers make a major announcement.

With the help of some devoted friends, a retired safecracker, and a Japanese currency trader, Sarah uncovers the leaks. But her discovery comes at great emotional expense and, more horribly, costs the lives of some of the people she loves. At times, Sarah seems a little too smart and a little too perfect, but Davies imbues her with a satisfying moral complexity. Sarah makes a very profitable personal trade on information gathered in her probe, for instance—and she doesn't give it back or use it to shelter the homeless.

Michael Ridpath's *Free to Trade*, also set in London, gets off to a decent start when Paul Murray, a young bond manager and former Olympic runner, learns that a female colleague has been found floating in the Thames. Murray is convinced she was killed because she learned something unseemly about one of their company's investments. Turning sleuth, he follows a trail that leads to New York, Phoenix, and Las Vegas. By the middle of the book, however, the plot is foundering and the reader, weary as the jet-lagged hero, is wondering whether it's worth going on. I did, but I probably wouldn't have if I had already read *Bombardiers* or *Vipers*, both of which are far better books.

BY JEFFREY M. LADERMAN

Senior Writer Laderman covers the financial markets.

BOOK BRIEFS

THE WARREN BUFFETT WAY

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Warren Buffett is a phenomenon—one of the savviest investors of the past half-century. Stockholders in his holding company, Berkshire Hathaway Inc., have seen per-share book value grow at an astounding annual rate of 23.3% in a 29-year period.

But Buffett's legend depends on more than a stunning investment record. Hedge fund operator George Soros and

former mutual-fund manager Peter S. Lynch are also stellar investors. It's only Buffett, the folksy, unpretentious billionaire, who's seen as a hero. In an era of hot money, derivative securities, and gunslinging money managers, he seeks out good companies and invests for the long haul. He steers clear of fads, makes deals worth hundreds of millions on a handshake—and seems to mint money.

How does he do it? For years, Buffett has been sharing his philosophy and strategies in BH's annual reports. Now, Robert Hagstrom Jr. usefully collects for the average investor much of that material, extrapolates Buffett's major tenets and illustrates each with examples from BH's portfolio. Hagstrom didn't interview Buffett for *The Warren Buffett Way*, but he did send him copies of what he was writing, since Buffett had to approve the use of material from the annual reports.

Hagstrom nicely lays out Buffett's value investment strategy, a marriage of quantitative financial discipline and shrewd judgments about management. And he explores Buffett's strongly held beliefs: Don't diversify. Ignore market swings. Don't worry about the economy. Buy a business, not a stock. Evaluate a company as a potential owner.

Perhaps Buffett's mystique accounts for *The Warren Buffett Way*'s best-sellerdom, for the book itself is plodding and worshipful. That contrasts with the annual reports, in which Buffett comes across as brilliant, erudite, and curmudgeonly. What's more, Hagstrom makes clear how much work and knowledge goes into Buffett's investing, which is to say—even given these insights, the average guy can't do what Buffett is able to do.

Buffett is well aware that the demands of job and family mean many people can't learn enough about business economics to follow his example and uncover sensibly priced companies with important long-term competitive advantages. For them, he recommends index funds and dollar cost averaging—and says they'll still outperform most investment professionals. "Paradoxically," says Buffett, "when 'dumb' money acknowledges its limitations, it ceases to be dumb."

Like many investment books, *The Warren Buffett Way* is best skimmed and kept as a reference. When a broker calls with a hot tip or your neighbor recommends a high-flying mutual fund, you can take it down, read some of Buffett's scathing insights into the market—and save yourself a bundle.

BY CHRISTOPHER FARRELL



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.....

BY STEPHEN H. WILDSTROM

PHONE CIRCUITS TO THE FAST LANE

In 1984, the IBM PC AT was the hot new personal computer. A modem that could send and receive data at 2,400 bits per second was considered blazing fast. And the Baby Bells, just spun off from AT&T, attracted little attention when they sketched their plans for a high-speed communications future called the Integrated

updates that will make ISDN easy to use.

ISDN runs over the same wires as what the phone companies refer to as "Plain Old Telephone Service" (POTS), and the telephone installer follows the same procedures used to add a regular line to your home or office. But the similarity ends there. A POTS line can

and disconnect as needed.

So if ISDN is so great, why does Bellcore, the research arm of the regional Bell companies, estimate that there are a mere 400,000 of such circuits in use, compared with the hundreds of millions of POTS lines?

The biggest reason is that ISDN remains user-hostile. A customer ordering the service will be stopped cold when the telephone company asks how the line should be "provisioned," a technical issue that depends on the equipment being used. New terminal adapters, such as the \$500 TA-210 from Motorola Inc., offer simplified set-up, but they're still a lot more complicated to install than modems.

At least one phone company has a good idea of how to bridge the gap.

Later this year, Ameritech Corp. will begin offering its Great Lakes area customers a \$399 package that includes a Motorola terminal adapter, installation, technical support, and software developed by Bellcore to make ISDN easier to use. In Illinois, a line will cost less than \$35 a month plus 5.2¢ per prime-time call. In Maryland, I pay Bell Atlantic Corp. \$36 a month plus 5¢ per minute, compared with a flat \$23 a month for a residential POTS line.

With Internet service providers beginning to offer ISDN, high-speed Net-surfing is the easiest way to experience the new digital service. But before ISDN can really hit the big time, it must become easy to use with popular remote E-mail and network-access programs. Today, ISDN users have to iron out compatibility issues on their own. This is no minor problem, but it could be solved quickly once users and equipment manufacturers demand solutions from software publishers. Then ISDN can really take off.

carry a single voice conversation or data at a maximum of 28,800 bits per second. An ISDN line provides up to 128,000 bits per second for voice, data, audio, or video in various combinations.

Transmission speed isn't the only benefit of an ISDN line. Experimenting with calls between my home and office, I found it took an average of 30 seconds to connect using a conventional modem. Using ISDN took me less than 5 seconds. And an ISDN terminal adapter, the equivalent of a modem, works without the modem's annoying bleeps and squawks.

A telecommuter with ISDN at both ends can work as though connected to an office network. The link will silently and swiftly connect

Services Digital Network.

After more than a decade of being derided as "It Still Does Nothing," ISDN's hour has come at last. Telecommuting, which can involve frequent access to E-mail and moving big, graphics-laden files, is probably the most important reason. Videoconferencing and Internet surfing have also helped create a market for fast digital communications.

MODEM OPERANDI. On the supply side, telephone companies are making the service cheaper and easier to get, and the starting price of the equipment needed to connect a computer to them has fallen from around \$2,000 a year ago to less than \$500 today. All that's needed now is one crucial element: Software

BULLETIN BOARD

ONLINE SERVICES

GRAPHICS TRAFFIC JAM

Did you ever wonder what happens while your online service tells you to wait for new artwork to be added? Reader Michael Di Clemente of New York did. He learned that the artwork makes

Please wait: Adding art

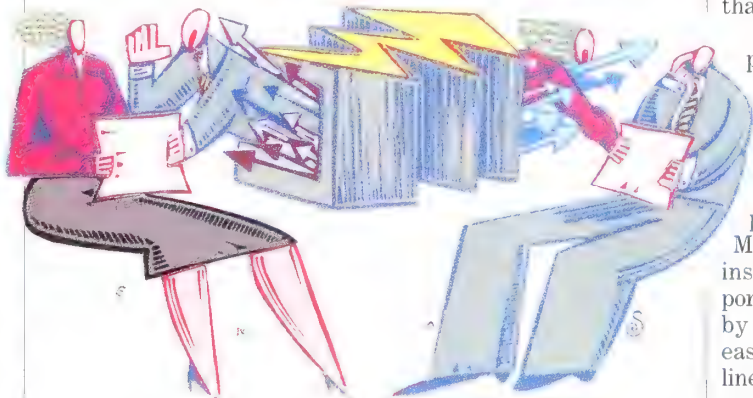
75%

viewing graphics faster in future visits but takes up permanent space on your hard disk. The problem is worst with America Online which stores the graphics in one big file that cannot be deleted. CompuServe saves the images as individual files. Prodigy saves only the most recently used graphics. Several megabytes of graphics are unlikely to be much of a problem on a typical desktop machine but could be a hassle on the less capacious hard drives of laptop computers.

SOFTWARE

HYPERTEXT TRANSLATOR

Tools making it easier to prepare documents for the Internet's World Wide Web continue to proliferate. The latest is WordPerfect Internet Publisher from Novell (800 451-5151). This free add-on allows users of WordPerfect 6.1 for Windows to automatically convert documents into the hypertext markup language required for the Web. The program should be available in the second quarter



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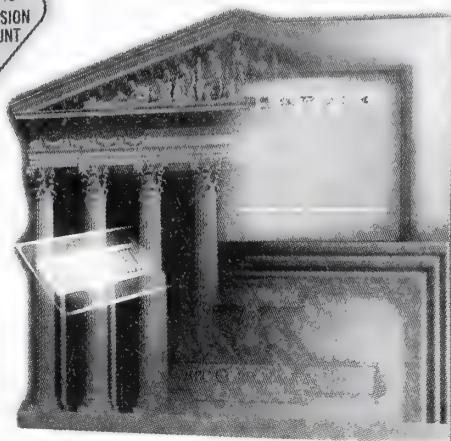
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BY PAUL CRAIG ROBERTS

IT'S TIME TO PRIVATIZE SOCIAL SECURITY



WHY WAIT?
Soaring entitlement costs will force the U.S. to break its word. Here's how to phase out Social Security as a federal program

The balanced budget amendment, which has passed the House, will turn out to be an exercise in futility—or a ramp to major tax increases—unless Congress takes a hard line against the growth of entitlements. The Clinton-appointed Bipartisan Commission on Entitlement & Tax Reform concluded before closing its doors on Jan. 31 that by 2028, federal spending on entitlement programs—principally Social Security, Medicare, and Medicaid—will exceed tax revenues, leaving nary a cent for interest on the debt, defense, or anything else.

To put the growing cost of entitlements in perspective, the budget President Clinton submitted to Congress on Feb. 6 projects that by 1997, Social Security, Medicare, Medicaid, and Health & Income Security (mainly but not entirely entitlement outlays) will comprise 56% of all federal spending and 64% of total federal revenues.

If those four budget categories are combined with defense expenditures and net interest paid on the federal debt, they will exceed total federal tax revenues in 1997 by \$1.6 billion. The deficit funds the rest of the government. Obviously, Senate Democrats are asking a legitimate question when they inquire of Republicans what they propose to cut in order to balance the budget.

NO FAITH. But there is more at stake than the budget. The growth of entitlements is a direct threat to the quality of our health care. The continued growth of Medicare and Medicaid—at twice the rate of 1994-97 federal tax revenues—will eventually force government to renege on its promises. One way of reneging would be to socialize health care in order to ration the delivery of services.

The government is already reneging on its Social Security promises by taxing the benefits. In the 1980s, the law was changed in order to make 50% of Social Security benefits subject to income tax, a figure that Clinton raised to 85%. Currently there are proposals to further curtail the benefits by raising the retirement age to 70 and by holding cost-of-living adjustments below the inflation rate. Ultimately, Social Security is doomed, since the ratio of workers to retirees is shrinking, and the implied hike in the employment tax would price U.S. labor out of world markets.

Judging from a recent poll, confidence among the young in the Social Security system is practically nonexistent. Only 9% of

those surveyed, who are between the ages 18 and 34, believe Social Security will have the money to pay their retirement benefits. A smaller percentage than believes in UFOs. A piecemeal approach to the budget simply passes a sinking ship on to the next water. Tax increases have been tried and have failed. Despite the higher income tax rates enacted by both Bush and Clinton in their respective "budget deals," Clinton's latest budget projects \$200 billion deficits indefinitely.

FACE SAVER. Entitlement promises have been undermined by the aging population and the perverse incentives of government handouts. It's time for politicians to face facts and to downsize government rationally. One way out of the entitlement mess would be to privatize Social Security. Since the young are disenchanted and would abandon the system given a chance, general revenues would have to be used to fund retiree benefits during the transition. But with \$200 billion deficits and no general revenues are available.

At the current rate of revenue growth, it would require a three-year budget freeze to balance the budget. Alternatively, the budget could be balanced over a longer period by holding spending growth below revenue growth. Clinton's budget projects average annual revenue growth of \$73 billion over the 1995-2000 period. If new-spending growth were held to \$40 billion annually instead of matching revenue growth, the budget would be balanced in six years.

Once the budget was balanced, holding spending growth below revenue growth would free revenues for phasing out Social Security. This is not an undertaking beyond our ability. Office of Management & Budget Director James C. Miller III essentially froze the budget in 1987. Chile has achieved a successful transition to a private retirement system, and Argentina has begun the privatization of its Social Security system. These nations do have skills that we lack, and they were beset by worse crises.

If politicians bite the bullet now, the transition can be made without the government having to repudiate its promises and without worsening the competitive position of American labor and capital in international markets. The alternative is to lurch from crisis to crisis, abandoning commitments on an ad hoc basis and destroying the credibility of the U.S. government.

Paul Craig Roberts is John M. Olin Fellow of the Institute for Political Economy and Distinguished Fellow of the Cato Institute in Washington, D.C.

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BY GENE KORETZ

CURING U.S. SAVINGS WOES

Don't count on aging boomers

For years, economists worried by America's low savings levels have pinned their hopes for an upturn on the aging of the baby boomers. In this view, the current savings slump that began in the mid-1970s largely reflects life-cycle consumption patterns as the boomers entered adulthood and devoted the bulk of their incomes to acquiring the material possessions needed to establish families and households.

In the years ahead, however, the baby boomers will start to focus on retirement needs, and by 2010, the whole generation will be in the high-saving, 45-64 age bracket. As these big spenders become big savers, America's saving shortfall could disappear.

The problem with this scenario, contend economists Richard Cantor and Andrew M. Yuengert of the Federal Reserve Bank of New York, is that it's not very likely. Although they expect boomers' savings rates to rise sharply with age, their projections indicate that the impact will be reduced by a continuing high rate of early retirement and by rising numbers of households with relatively low savings rates.

Indeed, as the boomers' share of total U.S. households declines—by about five percentage points from 1990 to 2010 (chart)—the share of households headed by those 65 and over (who tend to spend their savings) will rise by the same amount. By 2010, the two economists conclude, demographic shifts by themselves will probably raise the personal savings rate to only 4.9% of disposable income, up from 4.1% last year. This is a far cry from the 8.5% of the early 1970s.

Cantor and Yuengert also note that baby boomers appear to be richer than their parents were at similar ages, suggesting that their need for additional

savings may not be as pressing as some observers have claimed. Moreover, even if the boomers suffer future cuts in social security benefits, there's no guarantee they would respond by dramatically raising their savings rate.

None of this belies the fact that the nation as a whole has hurt its economic health by spending too much on consumption while saving and investing too little. The economists' message is simply that demography alone is unlikely to solve America's serious savings shortfall.

WHY DO PEOPLE REALLY SAVE?

Gift-giving may be a big motive

If Americans are to be induced to save more, policymakers need to understand savings behavior. And as a study by economists William G. Gale of the Brookings Institution and John Karl Scholz of the University of Wisconsin in the *Journal of Economic Perspectives* suggests, such behavior is more complex than many observers imagined.

The original life-cycle theory of savings, developed by Nobel laureate Franco Modigliani, was that people accumulated assets in their working years mainly so that they could consume them in retirement. Back in the 1970s, economists began to realize that the so-called bequest motive—the desire to leave wealth to one's dependents and children—was also a powerful stimulus to salt away savings.

Gale and Scholz focus on another aspect of the savings puzzle: so-called *inter vivos* transfers, or transfers of assets between living people. While some bequests are accidental—in that they occur because someone died earlier than anticipated—all *inter vivos* transfers are intended and thus a clearer departure from the simple life-cycle model.

Not unexpectedly, the two economists' analysis of household financial data found that most of such transfers involve gifts to children or grandchildren. But they also found that *inter vivos* transfers (excluding college expenses) actually represent no less than one-third of all transfers and account for at least 20% of U.S. wealth.

All of this suggests that *inter vivos* transfers, like bequests, are an important motive for saving. It also implies that many future retirees could conceivably choose to reduce their gift-giving if they find their savings inadequate to support their lifestyles.

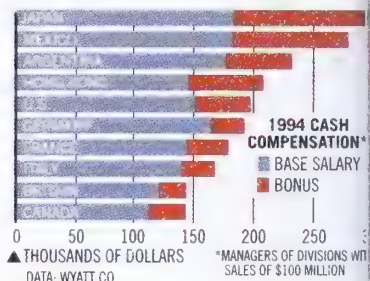
LOSING GROUND AT THE TOP

U.S. executive pay is lagging

It wasn't too many years ago that U.S. managers led the world in size of their paychecks. But in 1994, reports a Wyatt Co. survey, U.S. managers heading up \$100 million operations took home less than their counterparts in a number of countries, including Mexico. (The estimates in chart below reflect 1994 exchange rates, so Mexican pay is no longer so cushy.)

The dollar's decline since 1986 and recent U.S. pay restraint are two reasons

HOW MANAGERS FARE AROUND THE GLOBE



sons why U.S. managers have lost relative ground. Another is the economic explosion in emerging nations. For Americans still have one edge: They are among the few executives who use stock options, and Wyatt says that adding this to the tally would lift U.S. compensation closer to the top of the list.

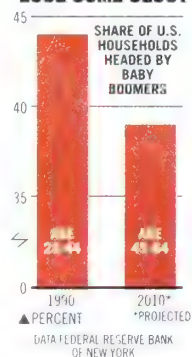
FINAL PAYMENTS ON THE BAILOUT

The total S&L cost: \$150 billion

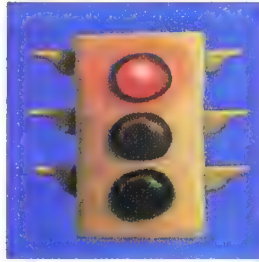
The savings and loan scandal that occurred after Congress rushed through legislation in the early 1990s to provide regulatory relief to the beleaguered thrift industry is history. But it's worth noting that the Congressional Budget Office's latest estimate of the net tab for the cleanup now winding down comes to some \$150 billion.

By comparison, the government spent \$17 billion last year for family support, \$10 billion for farm price supports, and \$7 billion for child nutrition. The scandal lives on today mainly as a component of the national debt. Its epitaph might well read: "Legislate in haste, pay the tax man in leisure."

BABY BOOMERS WILL LOSE SOME CLOUT



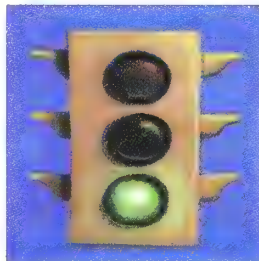
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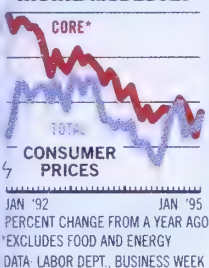
JAMES C. COOPER & KATHLEEN MADIGAN

WHY PRICE PRESSURES AREN'T SO PRESSING ANYMORE

U.S. ECONOMY

Face it. Inflation has changed. And with the economic outlook and monetary policy still focused on the trade-off between inflation and growth, it's time to take a closer look at why price pressures in the 1990s are different. What shows up are powerful structural shifts in competition, consumer behavior, and productivity that signal a new framework on which to hang inflation's hat. Certainly, inflation has been remarkably tame during this expansion, which is now almost four years old. Through the month of January, annual consumer inflation was only 2.8%, and the core rate, which excludes the often erratic pattern of energy and food prices, stood at a gentle 2.9% (chart).

PRICES ARE STILL RISING MODESTLY



However, was about half of its 5.3% pace at the end of the 1990-91 downturn.

Certainly, the traditional forces that have enabled businesses to hike prices in the past are starting to appear. Tighter labor markets are leading to faster wage growth. Higher capacity use raises the risks of production bottlenecks. And stronger economic growth around the globe has pushed up commodity prices.

ESE CYCLICAL FORCES

are why inflation is expected to creep higher this year and next. Indeed, the January consumer price index rose 0.3% from December, while the core index jumped 0.4%. That performance was worse than expected. It was fueled by a 1% jump in apparel prices after six months of decline, and a 0.6% increase in transportation costs, reflecting an upturn in airfares and another large gain in finance charges. Housing costs, up 0.4% in January, also rose faster, partly because of the 10.3% rise in postage fees.

But other powerful structural forces are overwhelming the cyclical pressures. This new inflation paradigm means prices in this upturn will peak at a much lower level than their high of 5.5% in the previous expansion.

The new look of inflation can be traced to changes in how the U.S. does business and shops, and how it competes with foreign rivals. Most important is Corporate America's push to lift productivity. Higher productivity levels have restrained the growth in unit-labor costs and actually lowered them in the manufacturing sector. Better output per hour worked at the factory also means that every rise in capacity use yields an even greater addition to output, diminishing the risks of shortages and bottlenecks.

Indeed, better efficiency is why increased production and rising operating rates have not yet touched off the usual wage-price spiral. Also, the Federal Reserve's past interest-rate hikes may be starting to slow industrial activity. Industrial output rose 0.4% in January after gains twice as large in November and December. In manufacturing, output rose just 0.3%, after the 1% increases in the two previous months.

Some of that slowdown might have been caused by an excessive buildup of inventories at the end of last year. However, the government's inventory data through December suggest that stock levels are in line with sales. Business inventories rose 0.2% while sales jumped 1.3%.

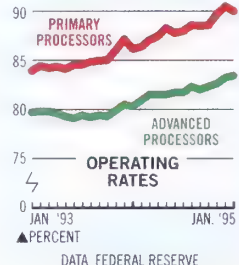
But despite the smaller gain in output, operating rates for all industry rose to a 15-year high in January of 85.5%. Rates in both primary and advanced processing have surged (chart). But because companies are more efficient now, shortages of goods have been rare, and customers have not had to accept higher prices to get supplies delivered.

LOWER UNIT-LABOR COSTS

have also given businesses some room to absorb rising commodity prices without too much damage to the bottom line. That's important because stiff competition from both domestic and foreign rivals has prevented most companies from passing along the higher cost of raw materials.

In its January producer price index report, the Labor Dept. states that prices for finished goods rose 0.3% last month, but the figure dips to just 0.2% when food and energy are excluded. Over the past year, the core PPI is up a mere 1.5%. That's quite a contrast to the 17.4% jump in raw-material prices and the 6% price hike

INDUSTRY USES MORE OF ITS CAPACITY



found in intermediate goods that have undergone some processing.

Businesses would have less trouble passing along price hikes if not for the striking shift in consumer spending patterns. In the austere '90s, consumers are simply unwilling to accept price hikes. This tightfisted behavior was fed by the same corporate downsizing that cut labor costs.

Moreover, there are many more demands on household incomes today—from contributions to pension plans to higher property taxes and savings for children's college expenses. And the budget squeeze will grow tighter this year as past Fed tightening boosts the cost of carrying credit-card balances and the monthly payments for adjustable-rate mortgages.

THE NEW AUSTERITY might not have gained a hold in the consumer psyche, though, if retailing itself had not changed. Consumers now can feed their bargain-hunting cravings at a vastly greater number of discounters and warehouse outlets than they could in the 1980s. Ten years ago, there were 755 Wal-Mart Stores and Sam's Wholesale Clubs. Today, almost 2,600 such stores dot the retail landscape.

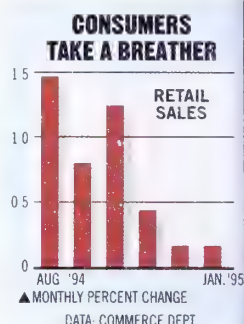
In fact, many retailers cited discounting as a reason for the lackluster pace of sales. Retail sales rose 0.2% in both December and January (chart). Merchants, especially department and apparel stores, had to cut prices

to move goods that just didn't make it as holiday gift.

Past Fed tightenings also played a role in keeping shoppers at home. Sales in January were weak for interest-sensitive items. Car sales fell 0.6% last month and furniture buying dropped 0.7%. This sluggishness should continue throughout 1995 as the seven rate hikes since February, 1994, work their way through the economy. As hiring and income growth slow this year, consumers will be even more resistant to price hikes.

But do the structural changes mean that the Fed's year-long inflation fight has been wrong? Even Fed Chairman Alan Greenspan noted in late January that the CPI overstated actual inflation from 0.5% to 1.5%. He said the upward bias meant that the U.S. is near price stability, but he added: "We are not there yet."

Indeed, the Fed is concerned not only with the level of inflation but with its direction as well. That is why policymakers will keep this economy on a short leash. Their strategy will work to keep the cyclical forces of tight labor markets and good shortages at bay. The new inflation paradigm will simply enhance the Fed's work and enable the U.S. to enjoy the best inflation decade since the 1960s.



AUSTRALIA

RATES MAY KEEP GOING UP DOWN UNDER

Higher interest rates are starting to take a bite out of Australia's rambunctious economy—but not enough to preclude more rate hikes.

The economy appears to have grown a robust 5.5% in 1994. Since mid-August, the Reserve Bank of Australia has lifted cash rates three times, totaling 2½ points, to 7.5%, in an effort to forestall inflation. Analysts see booming growth subsiding by the second half of 1995, but only if the RBA boosts rates even more.

However, given that hints of slower growth are already cropping up, the timing of the next rate hike is a bit cloudier. The jobless rate edged up to 9% in

January from 8.9% in December. Full-time job growth has slowed from its recent trend (chart), as have job ads. In December, retail sales fell for the second month in a row, and homebuilding permits dipped for the fourth month. A key leading indicator has been declining, and both consumer and business confidence are off their recent peaks.

But despite these signs of slowing, consumer spending and business investment outlays will continue

to power the economy in the first half, raising the RBA's concern about faster wage growth. Average weekly wages in the quarter ended Nov. 30 rose 4.2% from a year ago. That was the fastest

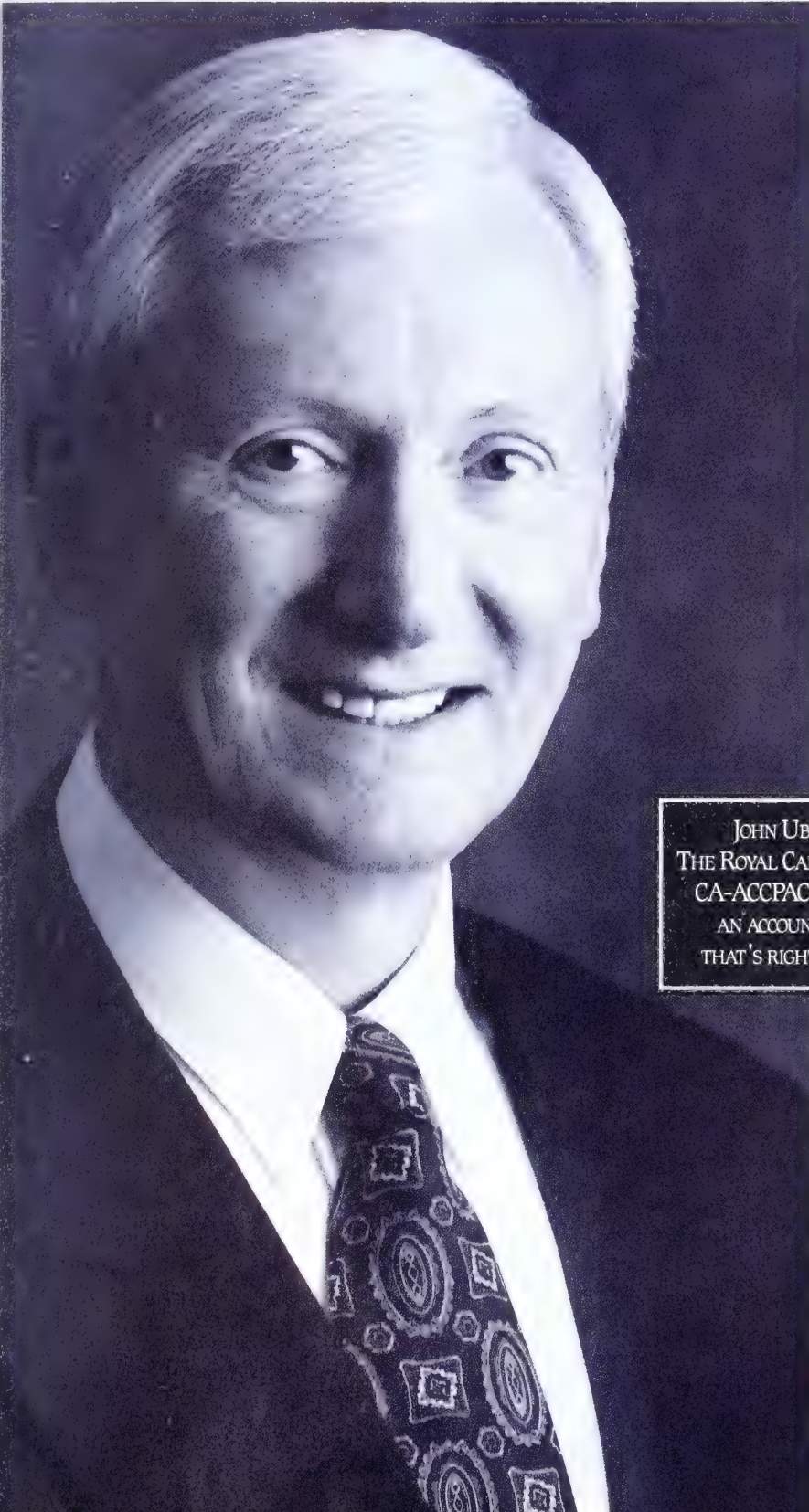
pace in nearly four years, and some of the larger wage negotiations were not settled until later.

Moreover, Treasurer Ralph Willis recently shook the financial markets when he announced there would be no midterm budget tightening, as the markets had expected. Willis also said the 1995 current account deficit will be some 45% greater than originally forecast. Indeed, the December gap widened 17%, to a record A\$2.4 billion. The Australian dollar, currently at 74.7 U.S. cents, has been in a slide for two weeks.

But the government may be building support for an even bigger package of tax hikes and spending cuts in its May 9 budget. In the meantime, though, that leaves policy solely to the RBA, and that can only mean higher rates—perhaps soon.



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SOFTWARE

Microsoft's rivals spoke, and the judge listened. Will his decision stand?

Microsoft Corp. seems to have finally met its match. The knockout punch came not from some powerful competitor but from U.S. District Court Judge Stanley Sporkin. On St. Valentine's Day, Sporkin nullified the consent decree the Justice Dept. reached with Microsoft last summer. The result of years of government investigation into Microsoft's alleged monopolistic practices, the decree had been decried by most of the software industry as ineffectual.

In the end, Sporkin surprised Microsoft's competitors by agreeing with them. "This certainly is good news," says Gordon E. Mayer, CEO of Geoworks, a small Alameda (Calif.) software company. "If the object is to increase competition, it is the right thing to do." Adds Stephen M. Case, CEO of America Online Inc.: "What I think is being said [in Sporkin's decision] is that this particular consent decree didn't go far enough."

ON A LIMB. Euphoria over the Sporkin decision may be short-lived, however. Scrambling to recover, the Justice Dept. planned a Feb. 16 announcement that it will appeal Sporkin's decision. If the decision is overturned, Justice antitrust chief Anne K. Bingaman will reinstate the consent decree she negotiated. "There's a good argument that the court exceeded its authority" by rejecting the decree, contends Washington antitrust lawyer Joseph Kattan. Even lawyers who normally would be against Microsoft agree. "I approve in concept with what [Sporkin] is saying," says prominent antitrust lawyer Maxwell M. Blecher. But he says Sporkin went out on a limb by trying to force Justice to bring more charges against Microsoft. "I think it will be reversed on appeal," he says. Justice seems confident: It has asked that the appeal be expedited—meaning a decision could come as early as late February.

Still, the Sporkin ruling is likely to slow the juggernaut approach of Microsoft Chairman William H. Gates III, who announced plans for a \$1.5 billion acquisition of financial software company Intuit.

GATES: Microsoft lawyers said they wouldn't renegotiate a consent decree.

SORRY, BILL, THE DEAL IS OFF

just weeks after the consent decree was announced. Some rival executives contend that the limited scope of the consent decree undermined—rather than chastened—Microsoft. Now they hope for a deal that gives Gates less latitude.

Indeed, the Sporkin opinion may inspire more rivals to push for a dismantling of the Intuit merger and other measures to slow Gates's entry into new markets. Justice's review of the Intuit deal is likely to be delayed by antitrust issues anyway. And Justice has asked the companies, including Lotus Development Corp., to comment on the merger. "The issues Judge Sporkin has raised about Microsoft's market position and industry dominance are real," says Thomas M. Abernethy, general counsel at Lotus. "It's positive that these issues will be further vented."

In rejecting the consent decree, Sporkin relied heavily on arguments advanced in an 11th-hour protest by Silicon Valley lawyer Gary L. Reback on behalf of anonymous clients (page 40). In a highly unusual move, Reback filed a friend-of-the-court brief on behalf of three companies that refused to identify themselves. Reback argued that Justice should have considered the fact that Microsoft's dominance will soon go away and operating systems because it can leverage its position there to enter such closely related markets as business applications and networking, home software, and online services. In short, it might largely be in control of the Information Superhighway (page 78).

Microsoft's opponents now hope the government will take steps to make that more difficult, if not impossible. "People said there was nothing we could do about Microsoft," says attorney Reback. "There it is and we've done it here. Now the question the government has to deal with is: How do we want the Information Superhighway to work?"

Still, Microsoft is far from K.O'd. In the wake of Sporkin's decision, Microsoft executives declined to say what they would do next. But the company has issued statements strongly agreeing with the opinion. After Justice files its appeal, Microsoft is likely to come back swinging, and try to help Justice get the decree restored.

In his 45-page opinion, Sporkin concluded that the decree was not in the best interest of the public for various

WHY SPORKIN NIXED THE MICROSOFT AGREEMENT



ANTICOMPETITIVE PRACTICES The judge contended the government and Microsoft "have been unable and unwilling adequately to address certain anticompetitive practices" the company has vowed to keep using

FEW COMPLIANCE MECHANISMS The settlement didn't adequately define how Microsoft would be made to comply with the deal's terms

INSUFFICIENT DETAILS The government did not provide sufficient details about its agreement with Microsoft

NARROW SCOPE The settlement should have been more far-reaching



BINGAMAN: Her best deal wasn't good enough

reasons (table). But the big surprise is his insistence that Justice should have brought more charges against Microsoft. He rejected the decree in part because Justice "was unable and unwilling adequately to address certain anticompetitive practices" that the decree did not mention. Further, he said, Microsoft was like-

ly to continue those practices. Foremost among the supposed tactics that concerned Sporkin is the allegation that Microsoft preannounces products that aren't ready for market to keep customers from buying similar ones from competitors. Justice rejected Sporkin's arguments. And it contends that turning over more information about its Microsoft consent decree—as he says it should—would jeopardize future settlements with other companies.

If Justice loses its appeal, its options in cracking down on Microsoft are limited. It could renegotiate a new consent decree. But that would require backpedaling by Bingham and Gates. Microsoft lawyers have insisted that they would not consider any other settlement, and Justice pointed out in a Jan. 20 hearing before Sporkin that after four years of investigation by the FTC and Justice, the decree was the best case it could make. Sporkin threw that out after a few weeks' review.

Justice also could try to prosecute the case in court. But even if Justice won at trial, legal experts say, it would probably lose on appeal. Preannouncing products is common industry practice, and courts in the past have failed to deter other companies—IBM, for example—from such tactics. And no court has ever successfully impeded a company dominant in one market from taking over another—making the argument that Microsoft is in danger of taking over the Information Highway a dubious one. "Those kinds of predictions, while plausible, are so uncertain that an appellate court would be very nervous about buying it," says William E. Kovacic, an antitrust law professor at George Mason University.

MICRO-BASHING? Much of the software industry would be happy just getting an airing of their grievances against Microsoft. Software companies charge, for example, that Microsoft requires them to disclose their own product plans in order to get early access to its operating system, then takes their ideas and announces competing products. They also claim that Microsoft will cut them off from information if they publicly complain. A public trial, says one executive, "may change the public image of Microsoft" as a great American company.

But those charges have always been murky. If Bingham could not find enough evidence in a nonpublic investiga-

tion, would a public trial do any better? So far, few rivals are coming forward with public allegations against Microsoft, allegedly fearing retaliation. And some companies think the charges are overblown. "There's so much rhetoric and so little fact to support these arguments," says Symantec Corp. President Gordon E. Eubanks, "that close scrutiny would probably reveal poor business decisions

by competitors, rather than a conspiracy by Microsoft, is the problem."

If its appeal of the Sporkin decision fails, Justice's final option would be to drop its case altogether. But if the consent decree was a disappointment to competitors, that would be considered a disaster. So, rivals are left to hope that, whatever happens, the rising intensity of criticism of Microsoft's dominance will

cause it to moderate its push into new markets. "Microsoft will change its behavior in order to avoid possible confrontation," predicts Mayer. Wishful thinking. Perhaps. But Judge Sporkin has handed a potent argument to those who thought Microsoft was unstoppable.

By Richard Brandt in San Francisco with Catherine Yang in Washington, and Amy Cortese in New York

THE ATTACK DOG WHO TOOK A CHUNK OUT OF MICROSOFT

One Saturday last summer, Gary L. Reback turned on the TV in search of morning cartoons for his kids. Instead, he found Attorney General Janet Reno and Anne K. Bingaman, head of the Justice Dept.'s antitrust unit. They were announcing an accord ending the government's protracted inquiry into the business practices of Microsoft Corp. The settlement was "toothless," thought Reback, doing little to protect dozens of his Silicon Valley clients from what he believed were the giant's illegal tactics. Insists Reback: "What Microsoft is doing tears at the fabric of Silicon Valley."

At first, Reback simply stewed. Then, in December, he read transcripts of the hearings before District Court Judge Stanley Sporkin into the merits of the consent decree. Encouraged by the judge's tough questions, Reback led an 11th-hour campaign to familiarize Sporkin with his view of how Microsoft's power threatens smaller Silicon Valley rivals. And he seems to have made his mark: The language of Sporkin's decision largely echoes Reback's arguments.

ENEMY NO. 1. The boyish-looking Reback probably doesn't strike most people as the type who could best powerful Microsoft. But at 45, he could hardly have been better prepared for the case. Born and raised in Knoxville, Tenn., he worked his way through Yale University as a computer programmer—a job that forever hooked him on technology. In 1974, Reback earned his law degree at Stanford University. He started out practicing antitrust law

in Washington, but in 1981 returned to California to specialize in technology and the law.

Since then, Reback has handled his share of noteworthy corporate battles. He defended Borland International Inc. in a copyright-infringement suit that Lotus Development Corp. won in 1993. (The case is now on appeal.) He also helped Borland



REBACK: The lawyer enraged top trustbusters

and Cadence Design Systems Inc. win Justice Dept. approval for major acquisitions.

In taking on Microsoft, Reback began by circulating transcripts of Sporkin's first hearing to companies. Subsequently inundated with calls from griping software outfits, he signed on three of them and filed papers to Sporkin outlining industry opposition. But he did so solely under his own name, not those of his clients, who, Reback says, are as frightened of Microsoft as "witnesses at a Mafia hit." So Reback, a partner at the Palo Alto (Calif.) law firm of Wilson, Sonsini, Goodrich &

Rosati, has become public enemy No. 1 to Microsoft.

Reback hasn't just incited the enmity of Microsoft CEO William H. Gates III. At a hearing in January, Bingaman was so enraged by Reback's comments about the Justice Dept.'s ineptitude that she pounded her fist against the lectern in defending her case. But that hasn't cowed

Reback one bit. "The people in Washington are wholly ignorant of how Silicon Valley works," he says. "We don't think the Antitrust Div. was tough enough to stand up to Microsoft, so we have to."

ON GUARD. What do Justice's antitrust attorneys think about Reback? At a Jan. 20 hearing, they argued that he is an interloper whose complaints came months after the end of the 60-day comment period allotted by law. They say his allegations have been thoroughly probed—and rejected. Even in the software industry, support for Reback's efforts is far from universal. "He's writing that brief to get his name in

the papers," says one industry source. J. Paul Grayson, president of software maker Micrografx Inc., says he is irked that an issue he thought was settled is now up in the air. Overall, Grayson says, Microsoft has been good for the software industry because it established strong standards.

Whatever his motives, Reback now has emerged as the legal profession's chief Microsoft watcher. From now on, it seems, anyone with a complaint against Microsoft will know who to call.

By Richard Brandt in Palo Alto, Calif.

ENATOR DANGERFIELD?

y Pressler may be in over
head in the telecom wars

e gets no respect. Think of Larry Pressler (R-S.D.) as the Rodney Dangerfield of the U.S. Senate. It's 7 to see why: Despite winning a Rhodes Scholarship and earning a Harvard law degree (though twice failing South Dakota bar exam), he's prone to floppers. In his current crusade to off public tv, for instance, he has needed that the Corporation for Public Broadcasting spends 75% of its budget overhead. The real figure is 4.5%. South Dakotan colleague in the Senate Democrat Thomas A. Daschle, once asked about Pressler: "A Senate seat is a terrible thing to waste."

ime to cut the comedy. As the new chairman of the Senate Commerce Committee, Pressler, 52, is now one of the most important people in Congress. Just the U.S. communications giants: In the second half of 1994, outfits from T to HBO anted up \$475,859 for his 6 election war chest. The reason: Pressler is in charge of shepherding the overhaul of the 60-year-old telecommunications law that limits competition in converging telecom, entertainment, information industries. The changes will oversee, says former GOP Senator Howard H. Baker Jr., who is now the long-distance industry's head lobbyist, will affect more people and more dollars than almost anything else you can conceive of for this Congress."

The Senate looks to be the key battleground for shaping deregulation. Last year's proposal sailed through the House but is getting derailed in a highly partisan Senate. This year, House telecom committee Chairman Jack Fields (R-) is hammering out a bipartisan bill, which he expects to have ready by March. But the Senate remains contentious. Partisan bickering already is taking out. And there have been many disagreements even within the Republican Party over when local phone companies should be allowed into long-distance calling and over how much rate of cable-TV operators should receive.

LEADER CHIESS. After a month of negotiations with fractious colleagues, Pressler unveiled a GOP measure on Feb. 1 that would let local calling companies enter the long-distance market three years after its passage. Democrats entered with a much more restric-

Larry Pressler



BORN Mar. 29, 1942, in Humboldt, S.D.

EDUCATION Graduated Phi Beta Kappa in 1964 from University of South Dakota. Rhodes Scholar. Master's in government and law degree from Harvard.

MILITARY SERVICE Army lieutenant, Vietnam 1966-68.

POLITICAL CAREER Two terms in House, 1974-78. Elected to Senate in 1978. Ran brief campaign for President in 1980.

PERSONAL Drives John Deere tractors for fun, attends Bible classes.

tive version on Feb. 15. Now comes the horse trading. And telecom companies lack confidence in Pressler's ability to facilitate matters. He "makes Quayle look like Kissinger," carps an industry executive who has spoken to Pressler at length.

Pressler has no illusions about the difficulty of getting the Senate to agree. "It's like playing a game of chess with several players and any one of them can checkmate at any point," he says.

At least he has been able to bring the warring GOP factions together. One camp, consisting of Senate Majority Leader Bob Dole (R-Kan.) and Senators Bob Packwood (R-Ore.) and John McCain (R-Ariz.), favors immediately letting the Bells enter the long-distance business. Another, including Pressler and Senators Trent Lott (R-Miss.) and Ted Stevens (R-Alaska), wants to restrain the Bells until their monopolies end so that they can't unfairly subsidize competitive ventures.

ROOM TO MOVE. Swallowing hard, Pressler agreed to a measure that would let long-distance companies into local markets in one year and the Bells into long distance after three. The bill also would abolish most cable-rate regulation.

But the next step will be a lot tougher. The Democrats' proposal would continue to regulate cable rates and would free the Bells to enter new businesses only when they can prove that they've removed potential barriers to competition. But there may be room for compromise. Severing the cable part of the GOP measure would help. And to assuage long-distance carriers, lawmakers could extend the date for the Bells' entry into long distance by a year or so.

What's unclear is whether Pressler can cut such a deal. His efforts to get the long-distance carriers and Baby Bells to resolve their differences have gone nowhere. Washington insiders say that Pressler is considered a loner, not known for working with other lawmakers. He has sponsored virtually no significant legislation during his two decades in Congress.

What's more, Pressler's fragile ego makes him wary of Democrats he must bargain with, especially when he thinks they're usurping his prerogatives as chairman. At a gathering in December, for instance, he was miffed when Vice-President Al Gore launched the feds' first airwaves auction without noting it was a GOP idea. "It was embarrassing to be on the stage," Pressler says.

Lobbyists also worry about Pressler's penchant for shooting from the lip. He turned an offhand comment by a Bell Atlantic Corp. executive into firm interest in buying the Corporation for Public Broadcasting, prompting the phone company to distance itself from the idea quickly when Pressler mentioned it on *Face the Nation*.

Luckily, Pressler has some powerful allies on his side. Dole, House Speaker Newt Gingrich (R-Ga.), and the high-tech-oriented White House all are pushing for telecom legislation. With that kind of backing, Pressler may not need respect to succeed.

By Mark Lewyn in Washington

TAX POLICY

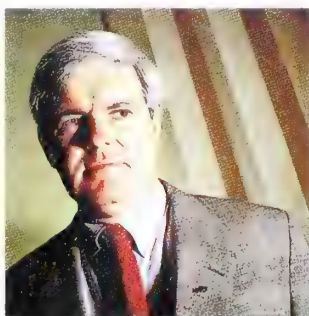
THE GOP'S TAX CUTS ARE FALLING OFF THE TABLE

The public is cool—and even business is unenthusiastic

A curious thing is happening to the huge individual and corporate tax cuts that are a centerpiece of the House GOP's Contract With America: Despite all the goodies, support among business and the general public is downright tepid. Many corporate executives say they'd much rather see Congress cut the deficit than taxes; they figure lower interest rates produced by deficit reduction would be more helpful than a modest drop in taxes. That's one reason Senate Republicans are rapidly losing interest in ambitious tax-cutting.

As a result of the shift, lawmakers may have to retool key provisions of the \$200 billion revenue bill—which would cut taxes on capital gains, expand individual retirement accounts, provide a more generous depreciation schedule for business, and hand most families a \$500-per-child tax credit. Even House Speaker Newt Gingrich (R-Ga.), chief author of the contract, hints that changes may be afoot. "I don't know of any backing down or backing off at all yet," he says, but adds: "None of these bills have to necessarily pass as written."

How will things turn out? The family tax credit and the individual capital-gains cut will still pass the House, although



GINGRICH: Already, hints that changes are afoot

the \$120 billion child credit could well be trimmed or delayed as Republicans struggle to find spending cuts needed to finance it. Now slated to go to families earning \$200,000 or less beginning in 1996, the credit could be phased in or offered only to those with a lower income. Plans to index capital gains for inflation and cut the rates in half may survive the House, but the

Senate is likely to be less generous with either the rate cut or indexing.

Business provisions of the contract are in worse trouble. The cut in corporate capital-gains taxes—now estimated to cost at least \$16 billion over five years—faces growing opposition. And the new depreciation system for capital equipment may be dumped. House Ways & Means Committee Chairman Bill Archer (R-Tex.) says the provision "has little or no support from the people who supposedly would benefit the most."

That's true for much of this bill. While Corporate America rarely passes up a chance to latch on to tax-cut bills, it has shown little enthusiasm for this one. And polls show that 60% of the public would prefer that Congress cut the deficit rather than trim taxes. In recent hearings around the country, House Budget Committee members

have heard the same message. One reason may be deep public skepticism over whether they'll ever see the benefits of the proposed tax breaks. "People don't support it because they don't believe it," says political analyst Kevin Phillips.

In the business community, there are some pockets of strong support—bankers and stockbrokers are pushing hard for generous new IRA deductions, and natural-resource companies love corporate capital-gains tax cuts. But for the most part, business is going through the motions merely as a courtesy to the GOP majority in Congress. "We're doing good soldiers," says one veteran corporate lobbyist. "But the truth is, there ain't a whole lot in this."

"NO PRESSURE." For many companies, other issues in the Republican contract take precedence over tax cuts. For instance, the National Association of Manufacturers has set regulatory and legal reform as its top priorities, with tax cuts well down on their wish list. In late January, the U.S. Chamber of Commerce polled its members on their legislative goals and got much the same response. Of their top 20 priorities, tax items ranked 12th, 14th, and 15th, well behind such issues as unfunded Social Security, paperwork reduction, and the balanced-budget amendment to the Constitution. Says one Senator who strongly backs tax cuts: "If you ask, they say they strongly support it, but they don't care if you do it. There's no pressure from business to cut their taxes."

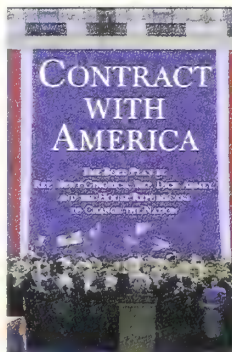
The contract makes some deficit-conscious execs downright uncomfortable. As much as Katherine M. Hudson, chief executive of Milwaukee-based industrial products maker W.H. Brady & Co., likes tax breaks, she wants spending cuts to come first: "We need some sort of deficit reduction in place so that tax cuts don't make the overall situation worse."

CONTRACT BLUES

The House is unlikely to follow on some tax provisions in its Contract With America, partly because the public's backing for the measures is eroding

WHAT THE CONTRACT PROMISED

- Establish a \$500-per-child tax credit for families earning \$200,000 or less
- Cut the capital-gains tax in half and index it for inflation
- Set a new business depreciation scheme as an incentive for capital investment
- Expand IRA eligibility



LEGISLATION THAT NOW IS LIKELY TO PASS

- The credit may be phased in or limited to families with a lower qualifying income
- The rate cut could be scaled back or indexing could be watered down
- The scheme likely will be dropped; business is pushing for relief from the alternative-minimum tax instead
- Some version should pass

The American Business Conference, which represents fast-growing midsize companies, also favors a capital-gains tax cut. But ABC President Barry K. Rogoff prefers that Congress tackle consumption-based reform instead of tinkering around the edges of the tax code. "We would much rather they do this kind of thinking in a broader package," says.

Representatives of big, capital-intensive industries are even less enthusiastic. The depreciation plan, for example, was supposed to be a boon for such busi-

nesses. But for companies that are constantly purchasing equipment, the cost-recovery proposal creates big problems. Gripes one lobbyist: "You're always in a cash-flow crisis under this thing."

Some businesses would rather see Congress water down the alternative-minimum tax, which often hammers companies when profits slide. Archer seems sympathetic. "We need to try to find some way to ameliorate the negative impact of the AMT on job creation," he says.

But financing AMT relief might be tricky. Under the curious rules of budget

accounting, dropping the depreciation proposal would cost \$18 billion over five years. So companies can't trade the plan for AMT relief. One option: Companies would forgo unused AMT deductions in return for future elimination of the tax.

Still, the bottom line is clear: So long as business and the public are cool on tax cuts, much of the GOP package could fade away by the time a bill reaches President Clinton's desk next fall.

By Howard Gleckman, with Richard S. Dunham in Washington and Richard A. Melcher in Chicago

CORPORATE PROFITS

IT DOESN'T GET MUCH BETTER THAN THIS

Corporate earnings were up a sizzling 41% last year

Southwood J. "Woody" Morcott had a good reason to crow on Feb. 13 when he announced Dana Corp.'s Q4 results. Earnings for the year leaped 78%, to \$228 million—Dana's best annual increase ever. Sales were up 21%, to \$6.6 billion. Morcott, the company's chief executive officer, attributes the auto-parts company's hot performance to global expansion and rising productivity. What's more, Morcott predicting that this year will be even better than last.

As it turns out, though, Dana's earnings—good as they are—weren't a whole lot above the norm. According to preliminary data compiled for BUSINESS WEEK's quarterly scorecard of corporate earnings for 900 companies, profits (pretax income from continuing operations before extraordinary items) were up an enormous 41% last year. That's the biggest jump since BUSINESS WEEK began compiling such data back in 1973—and it came on a sales increase of just 9%. Fourth-quarter earnings leaped 17%—the biggest rise since 1988's second quarter—on an 11% increase in sales. "This is the best profit environment by my reckoning in about 20 years," says Carmine J. Grigoli, chief portfolio strategist at Nomura Securities International Inc.

A BUMP. Why the stellar performance? Corporate America? Capacity utilization, at 85.5%, is at its highest level since 1979. That's largely because companies have chosen to eke out every inch they can from existing plants rather than invest in new ones. Detroit's Big Three auto makers, for instance, are using overtime to help juice output to the max. Another example is the steel industry. Buoyed by the strong

economy, it operated at 93% of capacity last year.

Corporate restructurings also are continuing to give profits a major bump. Manufacturing productivity jumped 4.6% last year, while wages only rose 2.3%.

IBM's turnaround alone added seven points to the BUSINESS WEEK 1994 profit index; the increase would decline to 34% if Big Blue were excluded from the list. DuPont Co. also is reaping the benefits of years of restructuring and sharp spikes in the price of basic chemicals. DuPont cut costs to the tune of \$3 billion per year. In the fourth quarter, its profits nearly doubled, to \$644 million, excluding extraordinary items, on sales that were up 9.6%, to \$10.1 billion.

Another company where restructuring is starting to pay off big is Westinghouse Electric Corp. Heavy cost-cutting and a strong international focus helped propel the company's power-generation and refrigerated-transportation businesses to a dynamic fourth quarter. That helped boost

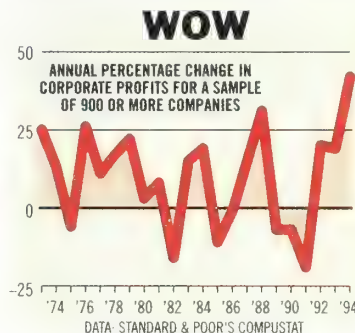
the overall company's 1994 net to \$77 million on revenue that was flat at \$8.9 billion—vs. a \$326 million loss last year. "We fundamentally changed how we do business," says Fredric G. Reynolds, Westinghouse's chief financial officer. "We're now competitive, and we're winning in the marketplace." Prospects for 1995 look good as well: As of January, Westinghouse had a mammoth order backlog of \$10.4 billion, up 5% from a year earlier.

SOME LAGGARDS. Of course, not all companies are seeing profit hikes. For one, heightened competition cut profits at usually stellar Southwest Airlines Co.

by 47% in the fourth quarter, to \$20.3 million. And doubts are rising about some hitherto booming industries: For instance, analysts are fretting about steel profits because a \$30-per-ton price hike on flat rolled steel instituted on Jan. 1 shows signs that it may not hold.

What's the prognosis for 1995? Market strategists expect profits to continue growing in the first quarter of the year and are optimistic for the full year. Grigoli expects earnings for companies in the Standard & Poor's 500-stock index to jump by 19% this year. That would be an excellent result—except by comparison with the colossal success of 1994.

By Lori Bongiorno in New York, with Stephen Baker in Pittsburgh and Joseph Weber in Philadelphia



Why such a stellar performance? Overtime is juicing output to the max, and manufacturing productivity is continuing to soar

COMMENTARY

By Mike McNamee

GIVE MEDICARE A STRONG DOSE OF MANAGED CARE

When Virginia A. Marhefka retired from Digital Equipment Corp. in 1992, she took a step stunning to Washington's lobbyists for the elderly: She dropped her traditional health insurance and joined a health maintenance organization. "I knew eventually I would need the kind of services I get from an HMO," explains Marhefka, who's a former software buyer in Clinton, Mass.

Her HMO, Fallon Community Health Plan, pays for preventive checkups, blood-pressure medicines, and a dietician to help her control her diabetes. Therefore, when she turned 65 in November, Marhefka refused to even consider abandoning Fallon for the standard Medicare insurance package, which wouldn't cover all those extra services she needed.

LOST LOVE. Mrs. Marhefka, please drop a line to Washington. For the capital's health and budget experts, it's an article of faith that seniors so love Medicare they wouldn't tolerate the slightest change. So, while Medicare's trust fund is going broke, politicians talk timidly about squeezing nickel-and-dime savings from doctors' and hospitals' fees. That approach would barely dent Medicare's soaring costs, let alone offer hope of controlling the federal budget.

Instead of tinkering, Congress should overhaul Medicare—now. Its models should be the Federal Employees Health Benefits Program and the pioneering benefit schemes of such companies as Digital and Xerox Corp. Congress should replace Medicare with a system of vouchers that seniors could use to choose any health plan that meets federal standards for quality and service. Most likely to prevail under such an ap-

proach would be managed-care systems, which provide more services for less money than does traditional Medicare.

Managed care's ability to limit health spending is constantly improving. In 1994, private companies saw their health-benefit costs per employee fall by 1.1%—the first drop in two decades, according to benefits consul-

easier to collect for a stay in the hospital than for services that would prevent hospitalization. The Medicare plan lacks such basics as prescription-drug coverage and a cap on out-of-pocket costs.

Medicare's own attempts to promote HMOs haven't made managed care widely available or attractive: Only 9% of Medicare's 33 million en-

rollees are in HMOs, and more innovative preferred-provider plans are available only as an experiment in 15 states. And under Medicare's pricing system, the bulk of managed-care savings go to the HMO—not to the government.

PLAY OR PAY. Medicare vouchers would offer seniors a clear choice: If they want expensive, uncoordinated fee-for-service medicine, they can simply pay the price. Most beneficiaries would probably decide to give cheaper managed-care plans a try. That could cut Medicare's double-digit spending growth rates in half, says economist J. D. Kleinke of the Baltimore-based health-researcher HCIA Inc.—trimming at least \$250 billion off the \$1.9 trillion Medicare bill between now and 2002.

Are America's politicians up to such an overhaul? "We are going to rethink Medicare from the ground up," House Speaker Newt Gingrich told the American Hospital Assn. on Jan. 30. However, Gingrich's lieutenants are focusing on minimal changes in premiums and benefits. If the Republicans want to achieve real savings—and to improve the health care that the elderly receive—they should be as bold as Virginia Marhefka and throw out an obsolete and out-of-control system.

McNamee follows health-care issues.



SAYING NO TO MEDICARE “I knew eventually I would need the kind of services I get from an HMO” — VIRGINIA MARHEFKA

phants A. Foster Higgins & Co. Some of the savings came from a dramatic rise in managed-care enrollment. But leading HMOs also are rooting out inefficient treatments and promoting preventive medical practices that promise to keep costs on a slow track in the future.

No insurer is riper for such changes than Medicare. Its benefits package—state-of-the-art for 1965—“promotes blank-check medicine,” suggests economist Linda A. Bergthold of the health consulting firm Lewin-VHI Inc. Under Medicare, it’s



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PEOPLE

UP FROM THE CEREAL AISLE

Ex-bag boy Ron Burkle is building a supermarket empire

Ron Burkle was just 13 when he began bagging groceries at his dad's store. He stayed with the grocery business, soaking up every detail. But 16 years later, after working his way up to vice-president of a local chain, it was his turn to get bagged: After bungling a \$100 million buyout of the company—despite persuading Warren Buffett to take a 50% interest—Burkle says he was fired on the spot.

Burkle's early stumble only whetted his appetite for action. "Getting fired was the best thing that ever happened to me," he says now. He's right. Today, Ronald Burkle, now 42, has emerged as a new power broker in the rapidly consolidating supermarket industry. On Feb. 6, his Los Angeles-based Yucaipa Cos. announced an agreement to acquire Dominick's Finer Foods Inc., a Chicago chain of 101 supermarkets, for \$750 million. That deal comes on the heels of a \$1.5 billion merger of Ralphs Grocery Co., a 168-store California chain, with Burkle's other Southern California holdings.

CONFIDENCE. All told, Burkle has rapidly built a \$9 billion supermarket empire of 570 stores in five states. His passion for operations and his confident pitchmanship have enabled him to complete a string of megadeals while risking relatively little of his own money. Instead, he relies on backing from the likes of Leon Black and George Soros. Black's Apollo Advisers put up \$100 million in cash to help finance the Ralphs deal; Bankers Trust Co. signed on to peddle \$2 billion of debt.

Investors say they have confidence in Burkle because he is as well versed in the ins and outs of grocery-distribution systems as he is at hawking a complex five-tranched LBO. "Ron is both a very good businessman and a very

good salesman. That's rare," says Stanley Druckenmiller, managing director of Soros Fund Management, which plunked \$50 million into an earlier Burkle deal.

Burkle describes his company as a "hybrid leveraged-buyout operation." Like an LBO fund, Yucaipa takes a healthy transaction fee—\$20 million in the Ralphs deal. But Burkle also sticks to what he knows and immerses himself in day-to-day operations. "We don't run this business from a

spruce up the fading chain in the midst of California's worst recession decades. Meanwhile, he began expanding his Food 4 Less warehouse stores. About 20% larger than regular stores, the 51 warehouses have automated receiving systems, allowing manufacturers to bypass costly distribution centers.

The strategy seems to be working. Yucaipa, a private company, reported combined operating cash flow of \$1 million in 1994, a 25% increase from the year before. Debt has climbed to \$1 billion, but the cash stream consistently doubles debt-service payments. And equity offering sometime in the next 24 months should raise more cash to pay off debt and fund expansion.

Burkle's next step: converting the Alpha Beta stores and several small chains into Ralphs stores, to compete head-on with Southern California's other two supermarket titans, Luc

BAGGING GROCERIES

Yucaipa's major acquisitions

		STORES	PRICE MILLIONS
1995	DOMINICK'S CHICAGO	101	\$750
1994	RALPHS LOS ANGELES	168	\$1,500
1994	SMITTY'S PHOENIX	28	\$138
1991	ALPHA BETA LOS ANGELES	142	\$271
1989	BOYS MARKETS LOS ANGELES	51	\$375

DATA: COMPANY REPORTS



CAPTAIN MUNCH: Burkle can't believe his good fortune

boardroom," says George Golleher, president of Yucaipa's Food 4 Less Inc. chain.

The morning after the Los Angeles riots, for instance, Burkle was on the phone with union leaders, assuring them he intended to rebuild three dozen South Central stores. In exchange for keeping workers on the payroll, Burkle got the unions to pitch in for health benefits, saving Burkle \$2.50 an hour on each of 2,400 workers. And the unions agreed to let Burkle assign workers such as meatcutters to cleanup duty.

Burkle broke into the supermarket big-time in 1991, buying 142 rundown Alpha Beta Co. stores for \$270 million from American Stores Co. He raised \$50 million in a private placement to

Stores Inc. and Vons Cos. Some deal makers wonder how long he can keep expanding. "Ron has done a good job bootstrapping his way up," says one adviser. "But when you're leveraged, you can always lose."

Burkle isn't worried. Last year, he purchased a \$20 million Beverly Hills mansion where he hosts gala fund-raisers for politicians and local charities. At his birthday party for Willie Brown, speaker of the California Assembly, Barbra Streisand showed up. Bill Clinton dropped by at a fund-raiser for Diann Feinstein. "Sometimes I pinch myself," says Burkle of his meteoric rise. No more bagging for this grocer.

By Eric Schine in Los Angeles

HIS IS WHAT THE FCC HAD IN MIND

Minority tax breaks helped build a mini-empire

When W. Don Cornwell left Goldman, Sachs & Co. in 1988 to build his own media empire from the ground up, he had more than a few eggs going for him. Cornwell boasted years of investment banking experience and a modest nest egg to put up capital. Wealthy friends—including attorney Vernon Jordan and talk-show host Oprah Winfrey—invested, too.

That Cornwell is African American would have posed a major hurdle to entrepreneurship in many other industries. In broadcasting, his race qualified for a Federal Communications Commission tax break meant to encourage minority ownership of broadcast property. That helped him build a vigorous public company called Granite Broadcasting Corp., which now owns seven stations in such midsize markets as Austin, Tex., and San Jose, Calif.

FOOT IN THE DOOR. The tax break is the same one that has caused a firestorm on Capitol Hill. At issue: Viacom's planned \$2.3 billion sale of its cable TV properties to black entrepreneur United W. Washington. The regulation also allows a seller to defer capital gains on a sale to a minority in hopes of making the deal more attractive. But in the Viacom deal, it meant that one of the nation's biggest companies could reap much as a \$600 million tax break, even though Washington owns only 21% of the acquiring company and is backed by giant Tele-Communications Inc.

Republicans in Congress are outraged at what they see as the cynical abuse of the system. So on Feb. 8, the House Ways & Means Committee voted to kill the program. The full House votes on the matter as soon as Feb. 21, and many legislators are pronouncing the tax break a goner.

Whatever you think of the Viacom deal or the FCC program itself, however, it clearly has paved the way for success in Cornwell's case: Granite has been smashing success. On Feb. 15, amidst all the Viacom-induced *Sturm und Drang*, Cornwell announced that operating cash flow swelled 50% in 1994, to \$25

million, on revenue of \$63 million. The stock has doubled in the past year, to around 7%. Says TV station broker Brian E. Cobb of Media Venture Partners: "He has earned the respect of other broadcasters."

Cornwell says the tax credit was critical to his early deals—mostly as a way for an upstart to get in the door. Those first buys, though, weren't exactly bargains. Despite help from the FCC, Granite paid more than 13 times operating cash flow for a Duluth (Minn.) station and 10 times cash flow for a Peoria (Ill.) station in 1988, while similar properties were selling at about 8.5 times, says broker Cobb. "In [anyone's] first deals, it's hard to get a serious seller to consider you," notes Lazard Frères & Co. analyst James P. Gorman, who follows the company.

The debate in Washington stems from a string of cases like the Viacom deal in which minorities appeared to be used as fronts for large corporations such as TCI, only to be bought out later. Cornwell, on the other hand, has won kudos as a hands-on operator who boosts profitability, usually by beefing up local newscasts and ad revenues. He has never sold a station and intends to keep buying until Granite hits the FCC limit of 14 stations. "Our company should be the poster boy" to illustrate how the tax break should work, he says.

Cornwell's clout means that his company will likely keep growing no matter what happens to the tax break. In a pending \$54 million acqui-



“In 1978, only 0.5% of the 10,000 broadcast properties were owned by minorities”

— W. DON CORNWELL, Granite Broadcasting Corp.

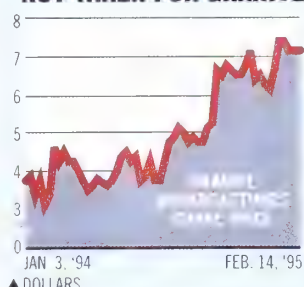
sition of a station in Kalamazoo, Mich., Granite is getting a \$7 million to \$10 million break on the purchase price. But Cornwell could easily pay the difference if Congress overrules the FCC.

And a likely acquisition of a Buffalo station later this year owes purely to Cornwell's dealmaking skills. In 1993, when broadcast values were depressed, Granite paid Prudential Securities Inc. \$7.5 million for Pru's 45% equity stake in the ABC affiliate. Granite also got a \$29 million note Prudential was holding on the property, which is collateralized by the remaining 55% of the equity. If the majority partner defaults, as is widely expected, Granite will control a station valued at about \$110 million.

SAVING DIVERSITY. So why does Cornwell care what happens in Congress? He would prefer to keep any financial advantage he has, of course. But it's more than that. "When the FCC program began in 1978," he notes, "only 0.5% of the 10,000 broadcast properties were owned by minorities." Now, the number is 2.9%. "To me," Cornwell says, "the harm is in the broader sense: Diversity is going to go away" if the tax break dies. It's up to Congress to decide if that's important.

By Elizabeth Lesly in New York

NOT TAKEN FOR GRANITE



DATA: BLOOMBERG FINANCIAL MARKETS

MARKETING

EYEWAY ROBBERY?

Contact-lens wearers pay through the nose for drops

You would expect to pay more per ounce for a product in a small package than a large one. But 8, 18, even 24 times more?

Such are the steep markups consumers pay for several brands of contact lens drops. The tiny eye-drop bottles contain the same ingredients as much larger solution bottles sold by the same companies, but are labeled differently and carry astronomical per-ounce prices.

"GRAND SLAM." Take Bausch & Lomb Inc.'s Sensitive Eyes Drops, which retails for about \$5.65 per 1-ounce container. The liquid inside is identical to Bausch & Lomb's Sensitive Eyes Saline Solution, which costs half as much (\$2.79) for a 12-oz. bottle. Similarly, OptiFree Rewetting Drops made by Nestlé S.A.'s Alcon Laboratories Inc. (\$6.99 for ½ oz.) is identical

IDENTICAL PRODUCTS, DIFFERENT PRICES

BAUSCH & LOMB

SIZE: 12 OZ.
PRICE: \$2.79
COST/OZ.: \$0.23

Sensitive Eyes

Sensitive Eyes

SIZE: 1 OZ.
PRICE: \$5.65
COST/OZ.: \$5.65

tical to Opti-Free Rinsing, Disinfecting & Storage Solution (\$6.99 for 12 oz.).

The scale of the differential amazes some marketing experts. "This seems to be the grand slam of finagling," says Jack Trout, a consultant. "It's not only a sneaky way to make money, but it's lousy marketing, the type of thing that backfires... when it's made public."

So far, it's not public at all. A Bausch & Lomb consumer help-line representative told an anonymous caller that Sen-

sitive Eyes saline and drops "are similar but the levels of concentration vary," though a B&L spokeswoman later conceded that the two products "share the same chemical formulation." An Alcon consumer representative told a caller that its Opti-Free drops and disinfecting solution are identical.

DROP ZONE. To be sure, manufacturers couldn't market their large-solution bottles as eye drops even if they wanted to. The Food & Drug Administration requires all eye drops to be labeled as such, and sold in small bottles. The FDA is concerned that contact lens wearers might drop the bigger saline bottles in their eyes, or might mix them up with similar-sized bottles of toxic cleansers.

But that doesn't explain why the tiny eye drop bottles cost so much. Part of the reason, says Bausch & Lomb, is that making the drops costs substantially more per ounce because of smaller production runs. But perhaps there's a simpler reason: Profit. Lens solutions carry average operating margins of 32%, says Jill Topkis, analyst at C.J. Lawrence. Deutsche Bank Securities. And margins on Eye Drops likely are higher—enough to set eye-popping prices.

By Mark Maremont in Boston

LEGAL AFFAIRS

SEE YOU IN CHINESE COURT

U.S. companies are fighting pirates on their home turf

Knockoff books, pirated software, black-market videocassettes—they're at the heart of the U.S. government's trade fracas with China. But as negotiators scramble to avert the imposition of sanctions on Feb. 26, some U.S. companies are quietly pursuing plans of their own.

Slowly, gingerly, they're sampling China's fledgling legal system. In the past year, American businesses including Walt Disney, Microsoft, and Harcourt Brace have filed as many as 25 copyright-infringement lawsuits in China's two-year-old Intellectual Property Tribunal of the Beijing Intermediate People's Court.

The companies expect little meaningful relief to come from this legal offensive. Nonetheless, they say, the

move represents an important step outside diplomatic channels for deterring piracy. "We never had any illusions that if we spent zillions of dollars bringing cases, we could stop the piracy," says Eric H. Smith, president of the Washington-based International Intellectual Property Alliance (IIPA). "But part of our strategy is to test the system."

Eighteen of the 25 cases have been brought in Beijing by the Business Software Alliance (BSA) on behalf of Microsoft, Lotus Development, and Autodesk. The BSA says that it will file several more copyright actions within weeks in cities such as Shanghai, Shenyang, and Chengtu.

At first, results from the legal strate-

gy were promising. Last June, following a flurry of lawsuits, 22 Beijing officials and U.S. company representatives raided six major computer-software dealers to seize evidence. Since then, the cases have "crawled along at a snail's pace," says Valerie Colbourn, Microsoft Corp. Hong Kong-based attorney.

PALTRY PENALTY. So far, indeed, Disney's copyright case is the only one to get a decision out of the new court. Last August, it ruled that two children's-publishing companies had illegally sold magazines featuring Disney characters. But the issue of monetary damages is unresolved.

Chinese officials say they're cracking down on counterfeiters. And a chief aim of the ongoing trade talks is persuading China to simplify legal procedures available to foreign interests. But two trademark-infringement cases lead U.S. companies to wonder how much progress they can expect. Both Disney and Microsoft have prevailed in those actions. But the actual awards, \$91 and \$2,600 respectively, will hardly deter future wrongdoing.

By Linda Himelstein in New York, with Pete Engardio in Hong Kong



FACE VALUE: Disney won a ruling against unauthorized use

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TEXTILES

A COMPANY THAT KNOWS HOW TO PUT OUT A FIRE

After a disaster, Milliken kept itself—and a town—in business



"TERRIBLE PROBLEM": The blaze wiped out a key carpet-making facility

After 23 years at Milliken & Co., Jean Railey suddenly finds herself working the third shift, inspecting carpets—a task she left behind years ago. The victim of another corporate downsizing? Hardly. Bailey took up her new job Feb. 6—six days after she watched her workplace burn to the ground. The La Grange (Ga.) plant flared on Jan. 31, and two weeks later 600 of the plant's 720 employees had new positions at Milliken facilities, some as far away as Britain and Japan.

The scene seems out of place in this era of restructuring and benefit cutbacks. Many companies would use a disaster such as the La Grange fire as an opportunity for write-offs and rationalizations. Not Milliken. Its response to the inferno at a key production plant demonstrates the payoff from effective disaster planning and strong customer ties. It's also a powerful, if anachronistic, image of small-town Southern paternalism—a company taking care of its company town.

OPPORTUNITY. La Grange, population 30,000, is a place that textiles have dominated from the time of the Civil War. Since the 1960s, textile money has paid to build half of every new church in town, much of La Grange College, and the county government offices. Closely held Milliken, with \$1 billion in sales worldwide, accounts for one in five jobs.

It was Milliken's Live Oak/Milstar

complex—which finishes carpet from eight other factories in town—where the fire started at 2 p.m. on Jan. 31, engulfing the plant in an hour. Alarms rang as far away as Lanett, Ala. And an urgent call sounded at Milliken's Spartanburg (S.C.) headquarters, where Chairman Roger Milliken was hosting a meeting of the company's 100-person contract sales force. Company officials raced to telephones, vainly urging the U.S. Forest Service to drop fire-killing chemicals on the plant's roof. Soon, however, Milliken learned the loss would be total. "We have a terrible problem," the 79-year-old grandson of founder Seth Milliken told his sales reps. "It's also a tremendous opportunity."

The opportunity: to show customers just how good a supplier Milliken could be. Two plane-loads of Milliken brass left Spartanburg that

afternoon for La Grange. Over the next four days, salespeople worked phones, contacting all 2,000 customers who might be affected. Getting the word out was critical. "Obviously, our competitors were going to be out there, telling everybody Milliken is out of business," says employee Robert Baird.

That evening, at Milliken's behest, Pont Co. had environmental specialists from seven states en route to La Grange. And by 3 a.m., company officials had organized 30 teams of Milliken employees to cover every concern, from personnel to reconstruction. Reports, complete with timetables, were due to Chief Operating Officer Thomas Malone by noon.

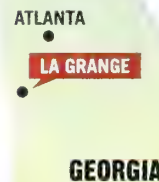
HEARTBREAKER. The next afternoon, Milliken employees gathered at the La Grange College gym for what many considered was their last company meeting. "I can't sit at home. I have to get back to work," fretted Greg Barnes, a 10-month Milliken worker. Malone told the crowd he was devastated by the loss. "I'm a gritty businessman, but this is my heart out," he said later. Malone promised jobs for as many as possible and immediate unemployment benefits for the rest. A ripple of excitement ran through the gym when Malone said the company would fly some production employees to work temporarily at the company's factory in Wigan, England.

Milliken decided to fly more than just workers. To reduce delays, it chartered planes to send semifinished carpets to the Wigan plant, essentially a twin to the defunct La Grange property. The fire wiped out five weeks of inventory, but Milliken promised to meet delivery deadlines for whatever critical needs could and refer customers it could not serve to other suppliers. La Grange plants worked around the clock to make up lost time. Two days after the fire, one of the company's biggest commercial accounts placed a \$250,000 order—a vote of confidence that rallied the town.

A week later, the La Grange High School band serenaded the first group of London-bound employees as they boarded a bus to take them to the Atlanta airport. Jean Railey watched as her son-in-law

Milliken dye mixer Philip Wilkerson left for his first trip abroad. "Everything went like clockwork," Railey says. "But I don't think I know anybody who doubted for a minute that it wouldn't go that way." In La Grange, Ga., that's the way things work.

By David Greising in La Grange, Ga.



Milliken quickly found new jobs for some 600 of the plant's 720 workers

TED BY KEITH H. HAMMONDS

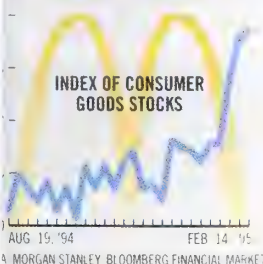
HAFFLER OM BUFFETT

A BOOK LAYING OUT HIS financial wisdom on the best-of list, investor-deity Warren Buffett has never had so many eyes on him. And on Feb. 14, the Omaha billionaire Buffett-watchers more gle. His Berkshire Hathaway holding company said it raised its stake in American Express to 9.8% from 7% at the start of the year and had purchased an 8.3% interest in Pittsburgh's PNC Bank. He also sought permission to buy more AmEx shares. As usual, Buffett didn't say why. Still, word is filings sent the stocks of AmEx and PNC higher and sparked a modest rally in other finance stocks.

CLOSING BELL

MAC ATTACK

Evidence of a slowing economy: Consumer stocks are up. The Morgan Stanley Consumer Stock Index is up 6.5% this year, versus 4% for the Dow Jones industrials. Leaders include McDonald's, up 15.5%; Rubbermaid, up 11.1%; and Wal-Mart Stores, up 12.4%. These companies won't boom in a slow economy—but they do tend to grow, while cyclicals such as automakers and homebuilders slow. Investors started selling cyclicals and buying household-name consumer stocks late in 1994.



IMPLANTS: ANOTHER DOW GETS BURNED

THERE ARE STILL BIG BUCKS to be made in silicone breast-implant litigation—despite the \$4.2 billion settlement reached last year between manufacturers and thousands of plaintiffs. On Feb. 15, a Houston jury ordered Dow Corning and Dow Chemical to pay a couple \$5.23 million—the woman got \$4.23 million, her husband the rest—after it found the safety of the devices had been “misrepresented.” The verdict is the first time Dow Chemical, which owns 50% of Dow Corning and must pay 20% of the award, has been held liable in an implant case. Now, lawyers are eyeing Dow Chemical as a new deep pocket to pick. The company asked to be dropped from the judgement.

JOE HILL, MEET THE NEWT

LABOR LAWS? A REPUBLICAN Congress? Not in the same breath. GOP legislators want to scrub the nation's labor rules, which they paint as outdated and inflationary. Their blitz began on Feb. 15 when committees in both Houses held hearings to attack the 64-year-old Davis-Bacon Act, which critics say makes Uncle Sam pay union wages on construction jobs. Lawmakers also aimed at a rule that sets minimum wages on federal service contracts. The Administration opposes the changes, saying the measures help maintain fair wages—but the President stopped short of promising a veto if Congress repeals the laws. “He’d have to see what the law says,” a Labor Dept. aide says.

THE COMDEX SHOW'S NEW SHOWMAN

HE KEEPS GOING AND GOING: On Feb. 14, Japan's Masayo-

HEADLINER: STEPHEN HANKS

FILLING BILL AGEE'S LOAFERS

The Boise bombshell dropped on Feb. 9: After years of uninspiring results at Morrison Knudsen, free-spending CEO William Agee was out. Stephen Hanks, 44, is in—for now.

Hanks, named interim CEO, is a Morrison lifer who spent 10 years toiling in the legal department before Agee joined the company in 1988. Then, Hanks won a string of promotions, becoming one of Agee's closest allies.

In the wake of the board revolt that forced Agee's departure, Hanks' old friendship seems a liability. His main asset: He knows the company, “and

he has been dealing with the banks,” says director Zbigniew Brzezinski. Morrison's banks have

threatened to pull \$225 million in loan covenants. And Hanks will have to fend off two shareholder lawsuits.

The new CEO has also restored regular staff meetings and is bringing back to Boise some of the operations that Agee had decentralized.

Many Morrison employees are happy to have an insider running the show, but some want a CEO with engineering expertise. So far, directors aren't tipping their hand.

By Dori Jones Yang



shi Son picked up another trophy. The 37-year-old billionaire entrepreneur, president of high-tech publisher Softbank, agreed to buy the annual Comdex computer show and 16 smaller ones for \$800 million from Interface Group. Last fall, Son paid \$202 million for the trade-show unit of Ziff-Davis Publishing after a failed \$1.6 billion bid for the whole company. Son made his fortune selling Japanese-language PC magazines and software packages to his information-hungry country. But he's eager to play a bigger role in the U.S. computer market.

LABOW TO TELEDYNE: I'LL BE BACK

WHX CHIEF RONALD LABOW has spent months eyeing Teledyne and its juicy \$860 million of overfunded pension assets. Now, rebuffed in

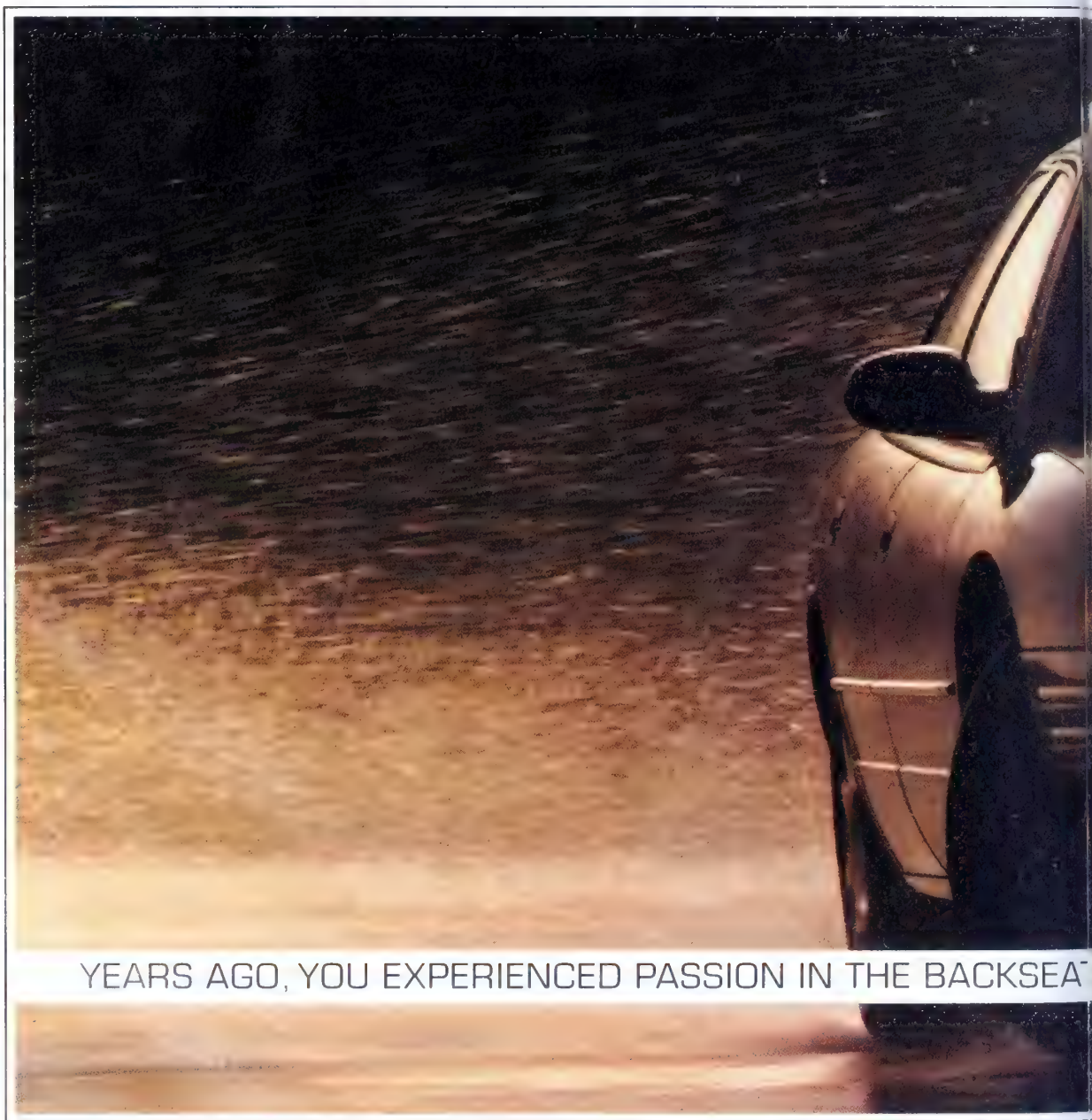
a \$22 per share, \$1.2 billion bid for the conglomerate, LaBow has made clear his plan to launch a proxy battle. It could get ugly: LaBow hopes to persuade disgruntled investors to elect a slate of four hand-picked candidates to Teledyne's board at the Apr. 26 annual meeting, giving him a majority. His goal: the “sale or merger of Teledyne to the highest bona fide bidder.” Like, say, Ronald LaBow.

ET CETERA...

- Five big airlines cut commissions to travel agents. One big agency sued.
- ITT keeps dumping assets. The latest financial units went to GE Capital for \$350 million.
- Piper Jaffray will pay \$70 million to investors in a derivative-laden bond fund.
- Saatchi's saga persists: The agency can't stop founder Maurice from starting a rival.



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YEARS AGO, YOU EXPERIENCED PASSION IN THE BACKSEAT

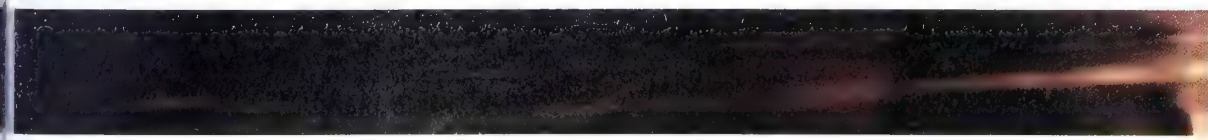
valve high-output V6. And the control of its
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OWEN ULLMANN

WHY GREENSPAN COULD BE UNSINKABLE

With the '96 campaign in full cry and the challengers jockeying for position, the smart money is bucking the conventional wisdom and betting on the incumbent, not Bill Clinton. Alan Greenspan.

The Federal Reserve Board chairman's term expires on June 2, 1996, just eight months before Election Day. The timing creates a dilemma for President Clinton and an opportunity for Greenspan. White House aides say Clinton would have the chance to name his own Fed boss to replace Greenspan, who has hiked interest rates seven times in a year. But Clinton stands little chance of naming a Democrat to the powerful post, which must be confirmed by a GOP-run Senate that's fast writing off Clinton as a lame duck. "The Republicans may refuse to hold hearings until after the election," says ex-Fed Governor Wayne D. Angell, Bear, Stearns & Co.'s chief economist and adviser to Senate Majority Leader Bob Dole (R-Kan.).

What's Clinton to do? Fed officials and some Presidential advisers believe he'll be forced to name Greenspan to a second four-year term—or keep the central banker on until after the election, when Clinton or his successor will have the right to name a new Fed boss. First chosen by Ronald Reagan in 1987, Greenspan was renominated by George Bush in 1991, but his confirmation was delayed by a Democratic-controlled Senate for six months. Fed insiders predict a similar stall next year if Clinton decides to dump Greenspan. "The Republicans smell blood," says one.

NEW LOBS. For his part, the savvy Fed chairman, who shows every sign of wanting to stay put, is doing what he can make the President feel comfortable. Although a lifelong conservative, Greenspan has been bonding with the Clinton Democrats from the Administration's first days. Remember him sitting next to the First Lady during the 1993 State

of the Union address? He often played tennis with former Treasury Secretary Lloyd M. Bentsen. And recently, he did a hard sell for the President's first Mexico rescue package.

But he hasn't forgotten his GOP friends. On Jan. 10, he gave them a belated Christmas gift: a painless way to cut the budget \$30 billion a year. Noting that the consumer price index overstates inflation, Greenspan told Congress that a recalculated CPI would cut cost-of-living hikes for Social Security and curb income-tax exemptions that rise with inflation. Although he has long favored changing the index, it was the first time the Fed chief put a price tag on the savings.

Democrats saw it as a blatant boost to the GOP, struggling to find \$1.3 trillion to balance the budget by 2002. "Shameless politicking," snaps one Clintonite.

WHO ELSE? Even if Clinton were determined to make a change, however, he lacks choices who could pass muster with Greenspan's many fans in the financial markets. Treasury Secretary Robert E. Rubin, an ex-Wall Streeter, has told friends he's not interested. Treasury Under Secretary Lawrence H. Summers, at 40, is considered too young—plus Congress blames him for not anticipating the Mexico crisis. The markets distrust

Fed Vice-Chairman Alan S. Blinder as an inflation dove. New York Federal Reserve Bank President William J. McDonough has the credentials, but Clinton doesn't know him.

With no obvious successor in the wings, the President could do worse than stick with Greenspan, who has managed a strong economy during Clinton's tenure. If Greenspan keeps the expansion going at a moderate pace without rising inflation for another year, the President might even win praise for staying the course. And that's certainly a better outcome than losing a nasty fight with the Senate and letting a Republican President choose the next Fed chairman.



HILL CHAT: Greenspan (right) with GOP fans John Kasich and Pete Domenici

CAPITAL WRAPUP

QUAYLE'S NEW QUEST

Dan Quayle may have pulled out of the Republican Presidential contest, but he won't assume the former Vice-president will be sitting on the sidelines throughout 1996. Associates say he's likely to run for governor of Indiana next year. Popular Democratic Governor Evan Bayh, whose second term expires in '96, can't succeed himself. Quayle, previously cool to the job, now sees it as a way to stay politically viable for a future race for the White House.

BANK REFORM HOLDUP

► Bankers' hopes of winning legislation to gain more access to the securities business are dimming. Although GOP leaders have introduced bills to repeal Depression-era laws separating commercial and investment banking, opponents are working hard to ambush the legislation. One example: Insurance agents are seeking a Senate amendment to retain state laws that bar banks from insurance sales. Such a provision would undercut bank support and kill reform.

LABOR GOES IT ALONE

► Several labor unions, miffed over the Democratic National Committee's dismal grassroots campaign last fall, may organize their own effort to recapture the House from the GOP next year. The \$2 million drive, led by service worker and government employee unions, would target Republicans who won close races in '94. Unions would set up networks of citizen activists who would publicize lawmakers' votes on such issues as the minimum wage and Social Security.

FRANCE

WILL *LES AFFAIRES* LEAD TO REFORM IN *LA FRANCE*?

A swarm of scandals could change the imperial style of corporate bosses and their political cronies

It should have been Edouard Balladur's day of glory—the formal launch of the French Prime Minister's seemingly unstoppable campaign for France's presidency. But as journalists jammed a Paris hotel on Feb. 13 to hear Balladur intone his sleep-inducing plans for an ailing nation, far more compelling political dramas were unfolding elsewhere.

In Lyon, a media glare inaugurated the trial of a local businessman accused of lavishing gifts on French luminaries to help the career of his father-in-law, Lyon Mayor Michel Noir, also a defendant. In Grenoble, a judge refused to free the city's mayor, in jail since October pending a slush-fund probe. And in Paris, key Balladur ally Interior Minister Charles Pasqua was embroiled in a kickback scandal. So Balladur got only fifth billing on the nightly newscast, well behind these updates on *les affaires*. That's what the French are calling the many bribery, political financing, and self-enrichment scandals that have dogged many politicians and executives for a year.

NO LETUP. The scandals are just part of the problems afflicting France, where everything from corruption charges to high jobless rates suggests that corporate and government institutions are adrift. The turmoil raises doubts about the leadership of France's ruling elite, which until now was trusted to run the country with no need for public accountability. Faced with the obvious necessity for change, France's elitist system "is still resisting," says Yves Meny, a French political scientist and author of a book on corruption. But he expects criticism of France's dense concentration of power to mount.

There's certainly no letup in the bad news. Banking giant Crédit Lyonnais is in need of its second government bailout

in less than a year. Despite efforts of France's best financial minds to stanch the losses, some \$18 billion in bad loans continue to hobble the company. Just one day after Balladur's speech, telecom blue chip Alcatel Alsthom had to deny another allegation of corporate misbehavior—that a subsidiary overbilled a French electric utility. The company is already facing charges that it massively overbilled France Telecom Group. Meanwhile, as the French read about corporate bailouts and allegations of wrongdoing, the economy as a whole is only meekly recovering, with joblessness at a stubbornly high 12.6%.

OLD BOYS. Although the French are worried about their jobs, they have not yet erupted in anger at their elected officials over *les affaires*, as happened in Italy last year. Partly that's because no top national leader has been tainted, and probes have produced few actual indictments—even though three Cabinet members have resigned and several corporate biggies have been questioned. Yet indictments and trials seem certain. The trial unfolding in Lyon is a precursor: Defendant Pierre Botton, a pharmacy executive, admits he spent \$2.8 million on vacations and favors for nearly a dozen of France's elite, including the country's top TV anchorman. But he denies illegally using his company's money to fund this largesse.

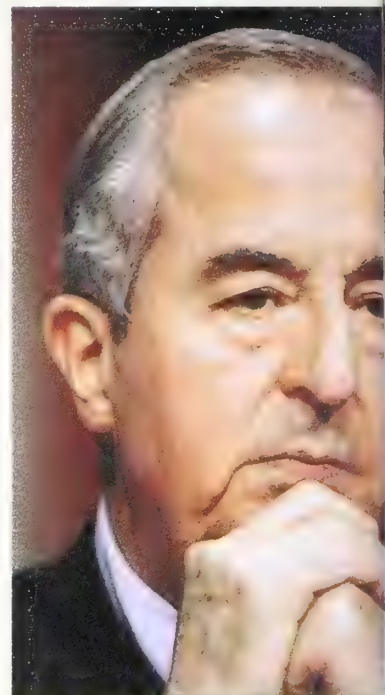
A thorough courtroom exposure of how France's elitist system operates could provide a much-needed jolt to Gallic complacency. Liberals are hoping for a debate on how all these problems—kickback scandals, failed government bailouts, poor economic performance—connect with each other within the French system of *dirigisme*. Guided by this interventionist policy, the national government has long exerted far more economic and social control than is possible in most of the world's developed economies.

Dirigisme has provided the sense of protection and order the French cherish. Yet it also blurs lines, fairly begging industry to curry favor. "Business and politicians are in cahoots," says Antoine

Gaudino, a private French fraud investigator. That's true especially at local levels. Observers aren't surprised that two companies that provide water and other municipal services have been at the center of several probes—Générale des Eaux and Lyonnaise des Eaux-Duméril. Crusading magistrates, meanwhile, are probing dozens of such questionable

Why France Is Adrift

The scandals are just part of the country's problems. With the recovery anemic, joblessness remains at a stubbornly high 12.6%. Banks are loaded with bad loans. All disturbs the French, long used to trusting a technocratic elite



ODDS ON: Balladur is the favorite

ls, throwing light on how France ks.

On the international level, the cozy nections fostered by the country's tectionist model are highlighting nce's competitiveness problem. Such ngements may have been accept- e in a closed economy managed, in emic Meny's words, by "a network xtremely competent people that has at difficulty in adapting itself to the rnationalization of the world econo-." The country's airline, computer, com, and other protected industries n doomed unless the French open their system to let market forces k.

France made strides towards chang- its system in the 1980s but never pleted the process. Yet rival Ger- y has started to accelerate its trans- nation under the pressures of unifica- and competition from Asia and the S. Says Philippe Claude, a French

venture capitalist at Atlas Venture: "The speed of change outside of France is accelerating quickly."

Meanwhile, the French keep making protectionist noises that seem increas- ingly out of place, as other Europeans commit to deregulating and opening their economies. For example, at a re- cent meeting in Bordeaux, European culture ministers shot down a French proposal to impose quotas on U.S. mo- vies and television programs.

THWARTED EFFORTS. France—and Eu- rope—need a strong leader in Paris to move the country away from protec- tionist leanings and clean up the cor- ruption. Yet so far, the evidence is scant that Balladur is that leader.

Sure, he's firmly pro-European, and he'll fight to protect the franc—key to monetary union. He's also privatizing French industry. But he has continued the wasteful French penchant for sub- sidizing weak "national champions" such

as computer maker Groupe Bull, Air France, and especially Crédit Lyonnais. He's also a pushover for special inter- ests. In late 1993, he fired Air France's chairman for resisting strikers' demands. In February, he cancelled a planned re- form of French technical schools after students took to the streets. That bodes ill for selling French opinion on needed social and fiscal change, says Albert Merlin, an economist at glassmaker Saint-Gobain.

It's still possible Balladur could grap- ple forcefully with France's problems, once he has an electoral mandate of his own. Backers say he'll continue nudging France toward free markets and will tackle deficits seriously. Yet his new program seems skimpy. To create jobs—his top goal—he would switch some wel- fare costs from employers to taxpay- ers, boost training, and encourage part-time hiring. "These aren't mea- sures—they're meausettes," says Phi-

lippe de Villiers, a right-wing splinter can- didate for the presiden- cy. Other French politi- cians don't have much more to offer.

The siege of scandals may yet lead to basic change. The govern- ment has outlawed cor- porate political giving. Shareholder activist Colette Neuville thinks a mood of accountabil- ity will spread in France, where corpo- rate brass often act like minor deities. Says Bernard Liautaud, the 32-year-old chief of Business Objects, one of France's few suc- cessful high-tech start- ups: "When executives fail, they should not re- bound to another com- pany, like in musical chairs," a game played repeatedly in France Inc.

Yet old habits die hard. It may take more serious *affaires* than have surfaced so far, along with setbacks out in the global market- place, before France's new rulers decide to make a clean break with business as usual. This is a crucial year for France.

By Stewart Toy, with Gail Edmondson and Bill Javetski, in Paris

▼ DIRIGISME State support of companies such as Crédit Lyonnais leaves France unready to compete globally



HIGH MAGISTRATES Judge Renaud Duymbeke is investigating illicit cal contributions



◀ SPECIAL INTERESTS Government finds itself paralyzed by demands from students, unions, and other beneficiaries of state spending



DATA BUSINESS WEEK

MEXICO

CEMEX: SOLID AS MEXICO SINKS

Its global reach and fierce cost-cutting are helping it to weather the crisis

Lorenzo Zambrano sits in his office in Monterrey, Mexico, and plugs his IBM ThinkPad into a desktop port. As CEO of Cementos Mexicanos (Cemex), he's checking up on his company's international operations. Although Cemex' main product is a basic commodity, its information system is definitely high-tech. With a keystroke, Zambrano calls up a bar chart plotting the previous day's erratic performance of a kiln in Venezuela and projects it on a big-screen TV set. He groans.

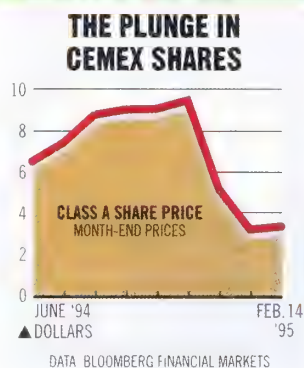
But another keystroke produces a smile. The graph of Kiln No. 1 at Balcones, the New Braunfels (Tex.) plant purchased last fall from competitor Lafarge-Coppée, shows that its downtime has shrunk to 5% from more than 20% when Cemex bought it last fall. "And this was a plant that was supposed to be very well-run, by a French company," Zambrano says, a bit smugly.

BIG SMILE. The maximum performance being squeezed out of Cemex' far-flung organization helps explain why the company is weathering Mexico's peso devaluation and ensuing economic crisis. Since taking over as CEO 10 years ago, Zambrano has helped Cemex extend its reach into 26 countries and acquire cement production facilities in six, including Spain, Venezuela, and the U.S. This year, the company is expected to cross a major milestone: non-Mexican operations will account for 51% of the company's \$3 billion in annual sales. That's why, despite being head of Latin America's most heavily leveraged company, Zambrano is smiling. "It will be tough for our Mexican operations but not for Cemex as a whole," he says.

Investors, including foreigners who held an estimated 20% of Cemex stock before the devaluation, have been taking a show-me attitude. Cemex shares, traded in Mexico City and over the counter in New York as American depositary receipts, plummeted to \$3.33 in mid-February, down from \$9.40 at the end of November (chart). The plunge reflected doubts about Cemex' ability to meet

payments on its \$3.2 billion hard-currency debt. "I was tremendously worried at first, until I ran through their numbers and saw it was feasible to service the debt," says Roberto Carrillo, who tracks Cemex for Baring Securities Inc. in Mexico City. "These guys know what they're doing—they know how to finance things." Baring still rates Cemex as a "buy."

Helping Cemex ride out the turbulence are the savvy moves it made in anticipation of a peso devaluation. Last September, for example, it issued a \$400 million convertible bond at just 4.25% interest to recycle short-term debt to a



more manageable three-year maturity.

But it is the cushion of rising hard-currency revenues from abroad (chart) that is giving investors the most confidence that Cemex will be able to handle the debt piled up by Zambrano in his global outreach. This year, Cemex expects that a shrinking \$580 million cash flow from Mexican operations

down from \$800 million in 1994, will be offset by a rising \$430 million flow from abroad, up from \$230 million in 1994. Baring CFO Gustavo Caballero: "Our diversification strategy has worked."

Of course, it could not protect Cemex against a complete meltdown of the



ican economy. But if Zambrano can the course, his company will re Corporate Mexico's coming of age. ican companies were challenged to ome world-class competitors by for President Carlos Salinas de Gor's opening of the economy to foreign le and investment.

Zambrano was among the handful entrepreneurs who responded aggressively, seeing open markets as an opportunity, not a threat. "We knew we to become an international company survive," he says. He had become of Cemex in 1985 at 41, after earn- a Stanford MBA and climbing the porate ranks for 18 years. Although Zambrano clan owns around 30% of nex' stock, it's not a family-run com- y, and he is the only member of his mediate family working in it.

PROFITS JUMP. Zambrano launched his ansion campaign by first snapping smaller Mexican cement companies. t what catapulted Cemex into the league was a \$1.8 billion move into ain, where Zambrano grabbed two nish cement companies in 1992 at prices and combined them into the ntry's biggest, Valenciana de Cemen-. Cost-cutting and stepped-up sales e yielded a handsome payoff: Last r, Valenciana's net profit jumped to 5.5 million, up from \$37.7 million in 83. After digesting Valenciana, Zam- ino moved to strengthen Cemex' sence in Latin America last April paying \$320 million for 60% of Vene- lan cement maker Vencemos.



NEW BREED
Zambrano is
among a
handful of
Mexican
business
leaders who
view open
markets as an
opportunity, not
a threat

It is this increasingly sophisticated, globalized operation that Cemex argues is giving it the means to pay its mostly dollar debt. With a projected cash flow of around \$1.1 billion this year, Cemex faces \$470 million in interest payments and \$690 million due on principal, plus \$160 million in operating cash requirements—a total of more than \$1.3 billion. But to cover these needs, Cemex has \$330 million

cash on hand, \$60 million in short-term investments, and \$500 million in committed lines of credit.

It helps, too, that CFO Caballero spent the past two years extending Cemex' debt to maturities averaging 4.5 years, up from 2 years when he began. "In Mexico unfortunately, it's always wise to be liquid and in a defensive position when there's a change of government," Zambrano notes. To further shore up its finances, Cemex is discussing with Citibank and J.P. Morgan & Co. a roll-over of existing "swap" loans totaling \$350 million that are backed by shares of Cemex and a Mexican subsidiary. And Caballero is looking at ways to borrow against \$500 million of assets of U.S. subsidiary Sunbelt Corp.

Although major expansion moves are now on hold, Zambrano hopes to return as soon as possible to building Cemex' global profile, even across the Pacific. Cemex' Hong Kong office is studying several ventures in China. "We'll be there, one way or another, in the next two years at most," Zambrano says.

SOME SKEPTICS. Such single-minded vision reflects three generations of Zambrano commitment to Cemex. Founded in 1906 under another name, the company was reorganized in 1920 by Zambrano's grandfather. When Zambrano returned from Stanford to join the company, he had to overcome skepticism: "People said I'd be a disaster because I was a family member." He quickly proved himself. Of the doubters, he says drily: "I fired a few people in the first few months."

Now, Zambrano, a lifelong bachelor, is enjoying the rewards of success with expensive hobbies such as collecting Ferraris and Latin American art. If he can navigate Cemex through Mexico's crisis, he'll be able to enjoy more than just a fancy lifestyle. He'll be able to say he firmly established Mexico's first true multinational on the world stage.

By Geri Smith in Monterrey and John Pearson in New York

As a result of all these moves, Cemex has become an influential player in a group that shapes the terms of competition in many markets. The club, led by Swiss-based Holderbank, includes France's Lafarge-Coppée and Italy's Italcementi as well as Cemex. The key battleground will be the emerging markets, where the Mexican group has real strengths. In Asia, for example, Cemex is stepping up exports with orders for 2 million tons in 1995 from Taiwan, Thailand, and Indonesia.

Underpinning these moves is Cemex' competitive cost structure and high worldwide operating margin of 26.8%, much better than rivals' average of less than 10%. Zambrano sent a 23-member "workout" team to Spain to slash Valenciana's costs. And last October, Zambrano unleashed the team on Cemex in

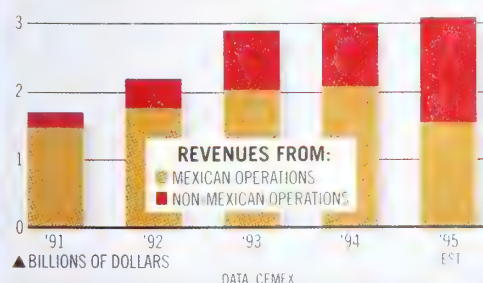
Mexico. It quickly identified \$85 million in annual cost savings.

A key to Cemex' competitiveness is its online information system. It links all of Cemex' offices in Mexico and abroad via a network of satellite dishes, leased lines, and microwave communications. Zambrano, who travels with his ThinkPad, and all other executives can obtain details on any of Cemex' worldwide operations. The system is crucial in managing Cemex' responses to market conditions. Referring to Cemex' Caribbean operations, competitor Gerald Essl, president of San Antonio-based Texas Lehigh Cement Co., says: "It's just phenomenal, the network they have and the flexibility of where to bring in product," he says.

CEMEX' GLOBAL OUTREACH...

COMPANY/ COUNTRY	YEAR	PURCHASE PRICE IN MILLIONS
VALENCIANA SPAIN	1992	\$1,840
VENCENOS VENEZUELA	1994	\$320
BAYANO PANAMA	1994	\$60
BALCONES U.S.	1994	\$105
PRODUCTORA NACIONAL NICARAGUA	Pending	\$12

...HAS REDUCED ITS DEPENDENCE ON THE MEXICAN MARKET

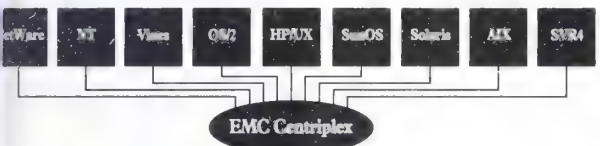


Everything A CEO Should Know About Data Storage:

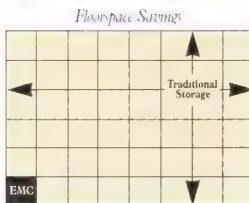
1. In 1994, 50% of your computer hardware budget was spent on it. 2. By the end of the decade, you'll spend 70% on it.

Everything An IS Manager Should Know (Now That The CEO Knows The Facts On The Left):

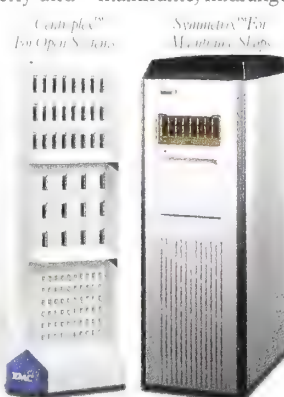
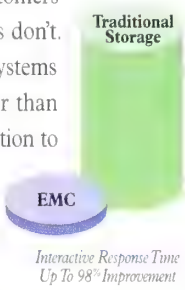
There is an avalanche of information now running through your company. It is growing. 2. The more information your company creates, the more information your company needs. 3. It's now tougher than ever to distribute, manage, store and protect the integrity of your information. 4. Successful companies are reorganizing themselves around the competitive use of information. 5. Chances are, your competition is using storage to gain competitive advantages. Not just to save money but to make money and to increase market



share. 6. For instance, by storing their information in central locations, companies are moving, managing and controlling their information more efficiently than before, and getting their products to market faster. The Gartner Group reports that roughly half of machine-readable data now reside on desktops. How well your company uses, leverages and protects its open client/server-based information will determine its performance. 8. EMC is the leader in data storage and retrieval systems. We focus all of our resources on this one area, getting the best technologies to you first, giving you an edge no one else has. 9. With the highest performance, capacity and availability, our systems will increase your profits, increase your market share, make your customers happier and ensure the integrity of your information. 10. EMC systems maximize the performance and value of your CPUs, your network and your software like no other storage available, extending the useful life of a CPU by several years. 11. We package best-of-breed cache, disk and memory technologies in a way that has revolutionized DASD—helping you manage information better while drastically reducing floor space requirements



and environmental costs. 12. Our systems' quicker response times improve customer service, transaction processing and overall employee efficiency. 13. Only EMC is able to offer the best storage technologies first because of our MOSAIC: 2000 architecture. This allows us to get the latest storage solutions to you faster, so your information is always being accessed faster and protected better than your competitors' information. 14. Since we're always first to market, our customers get competitive advantages their competitors don't. 15. Without compatibility problems. 16. Our systems get information into employees' hands faster than ever before, allowing them to use that information to make your company more successful. 17. Our systems not only provide faster access, they ensure that the information is secure, and always available. 18. Case in point: Symmetrix, the world's fastest and most highly available mainframe storage system. 19. Harmonix, a midrange storage system that makes an AS/400 scream. 20. And Centriplex, the first mainframe class, centralized storage designed specifically for open environments. 21. Our customers are experts at getting more value out of their mainframe, midrange and client/server storage systems. Because an EMC storage system isn't just passive storage. 22. It's part of a dynamic strategy for growth. 23. It isn't a commodity. 24. It's a value center. 25. It's a competitive weapon. 26. It's why EMC is a highly profitable Fortune 500 company and the world leader in storage solutions, producing only one thing: Storage. 27. Call 1-800-424-EMC2 ext.136 and learn how EMC can help you use information to improve your company's performance. 28. As well as your own.

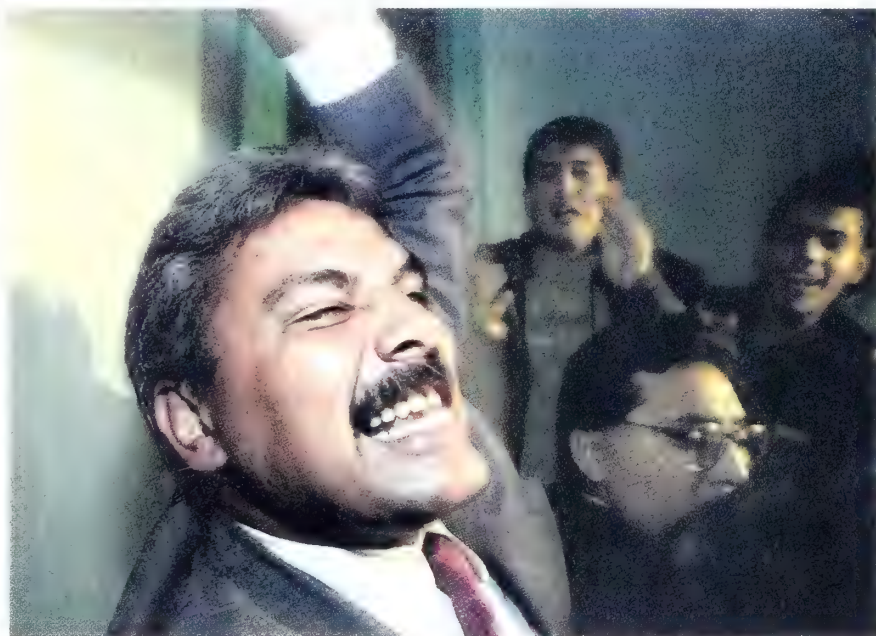


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MEXICO

THE VACUUM AT THE TOP IS GETTING DOWNRIGHT SCARY

Zedillo's paralysis is speeding Mexico's collapse



GLEE IN GUADALAJARA: *The PAN's Cárdenas celebrates his victory*

Two weeks after the U.S. cobbled together a \$50 billion rescue plan for Mexico, the crisis seems far from over. President Ernesto Zedillo Ponce de León's political moves are baffling both foreign investors and his own people. Voters showed their anger with Zedillo when they voted on Feb. 12 to oust his ruling Institutional Revolutionary Party from the governorship of the important state of Jalisco.

While Zedillo salvaged a measure of respect by promising to uphold the victory of Alberto Cárdenas of the center-right National Action Party (PAN), that isn't checking the fall of his prestige or the collapse of Mexico's economy. Zedillo seems paralyzed over how he will use the American money and how he plans to restructure Mexico's decaying finances. Talk is circulating in Zedillo's government of putting Mexico's monetary policy under the control of a so-called currency board, in effect taking economic policy out of his hands. "We are on the verge of seeing the economy explode into pieces," says Sergio Raimond-Kedilnac, the dean of Mexico's leading business school, the Pan American Institute of Higher Business Studies.

Indeed, the business community was rocked on Feb. 15 by Grupo Sidek's default on \$19.5 million in corporate IOUs. Sidek, a major tourism developer and steel producer, has \$100 million in dollar-denominated commercial paper coming due in the next two months and a total of \$980 million in dollar-denominated debt. Fears of other defaults shook the stock market, which was already plenty jittery over rumors that Banca Serfin, Mexico's third-largest, was under pressure. Another rumor, later denied, had it that Central Bank Governor Miguel Mancera was about to resign.

All this makes the markets very nervous. The peso and the *bolsa* are testing their lows, and interest rates are soaring. On Feb. 15, rates on 28-day Mexi-

"We are on the verge
of seeing
the economy
explode into pieces"

can treasury bills jumped 5%, to 40%

Business is grinding to a halt as expectations of a severe recession begin to bite. Construction is dead. New-truck sales plunged by 86% in January, and bus sales fell by 66%, according to the National Association of Bus, Truck and Tractor Producers. Mercedes-Benz shut its two plants for three weeks in January, and Grupo Dina plans to shut down production for 60 days this year.

Many other sectors of the economy are preparing for the worst. Companies involved in services, tourism, and trade got a shock when NAFINSA, the national development bank, told the National Association of Credit Unions this week that it was cutting off government credit to the thousands of small and medium-size businesses they represent.

QUICK FIXES. Executives are pleading for Zedillo to come out of his shell. Jorge Arganis, president of the Mexican Engineering Society, says Zedillo must act to keep thousands of businesses from going bankrupt. "He must do what the U.S. did after the crash of 1929—put people to work by spending whatever little money they have on public works projects, road repair—anything," Arganis says. "Zedillo is frightening investors—they must see us working."

Zedillo's advisers explain that he must negotiate the details of the rescue package with the U.S. before disclosing his intentions. But delay is sparking unease, even in his inner circle. Realizing how low the government's credibility has sunk, aides to Zedillo are pondering quick-fix measures that before would have been unthinkable. At least one of the vice-governors of the central bank is said to be pushing for the adoption of a currency board, an independent group that would fix Mexico's exchange rate to around five pesos to the dollar and in effect put Mexico's monetary policy in Washington's hands. Steve H. Hanke, a currency board theoretician at Johns Hopkins University in Baltimore, says the idea is being considered in Mexico at the highest levels of the central bank and in the government. Hanke gives it a better than 50% chance of being implemented. Some Wall Street professionals favor a currency board because it would promise a stable exchange rate and a more certain repayment of investors.

But most analysts think that Mexico is too complex to be cured by magic bullets. What's wanted is a sensible program and sound leadership from Zedillo. The former may be in the works, but there's little sign of the latter.

By Geri Smith in Mexico City, with Stanley Reed in New York

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next office will open up. You
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CANADA

MEANWHILE, TO THE NORTH, NAFTA IS A SMASH

The pact has sharply boosted U.S.-Canada trade—and growth

Critics of the North American Free Trade Agreement (NAFTA) have been having a field day since the Mexican peso hit the skids. But at best, they're only half right. Even as Mexico hunkers down, trade and investment between the U.S. and Canada is exploding. No wonder President Clinton is eagerly packing his woollens for a state visit to Ottawa on Feb. 23-24. The visit should offer Clinton, who once considered NAFTA his top foreign policy accomplishment, a chance to recoup.

But Clinton's first state visit to Canada will be far more than congratulatory speeches. Sure, trade between the U.S. and Canada hit \$260 billion last year, up 50% since 1988, when the U.S. and Canada signed a free-trade agreement that laid the groundwork for NAFTA. Now, both sides are eager to tear down barriers that still stand in the way of even greater trade. U.S. and Canadian negotiators are racing to complete a far-reaching "open skies" aviation agreement, which Clinton hopes to sign on Feb. 24. Beyond that, both sides are hoping to make progress in resolving trade disputes over everything from U.S. limits on Canadian wheat to Canada's decision to yank a U.S.-owned country-music TV station off the air.

MILLIONS FOR MINIVANS. Already, a surge of investments is linking corporations on both sides of the border as never before. The change is driven in part by the cheap Canadian dollar, which has plunged to just 71¢, down from a high of 89¢ in 1991. In autos, for example, it now costs "20% to 25% less to assemble a car in Canada than in the U.S.," says David Adams, director of policy for Canada's Motor Vehicle Manufacturers' Assn.

Such savings have the Big Three pumping billions into Detroit North. Ford Motor Co. of Canada has spent more than \$700 million to revamp its plant in Oakville, Ont., to produce Windstar minivans. And Ford is spending an additional \$1.5 billion to upgrade its Ontario truck and engine plants. Thanks to similar investments, Chrysler Canada Ltd. last year produced a record 695,000

vehicles in Canada—including most of its minivans and LH models. In all, Adams figures, Canadian auto plants now assemble 17% of all the vehicles produced in the U.S. and Canada, even though Canada accounts for less than 10% of the North American market.



Meanwhile, the overall surge in Canadian business investment has created some big opportunities for U.S. machinery makers. Last year, U.S. exports of machine tools to Canada more than doubled, to a record \$380 million. Business was even better for Giddings & Lewis Inc., the largest U.S. toolmaker, whose shipments to Canada tripled, while orders jumped fivefold.

The low dollar also is making it easier for U.S. companies to snap up juicy Canadian targets. On Feb. 7, Silicon Graphics Inc. announced it will spend \$365 million to buy Toronto-based Alias Research Inc., which developed the software used to create the special effects in *Jurassic Park*. And on Feb. 13, Nike Inc.

completed its \$390 million purchase of Montreal-based Canstar Sports Inc., world's largest producer of hockey equipment.

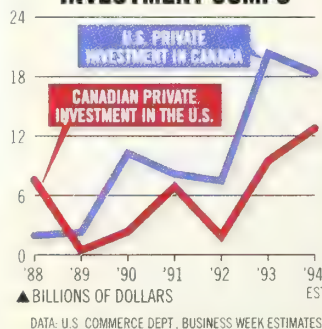
The pace of cross-border deals may even increase. Last year, U.S. companies spent a near-record \$3.9 billion to make 113 acquisitions in Canada, says consultants KPMG. That was matched by the record \$4 billion that Canadian companies spent to do 127 U.S. deals. Overall, private investment between the two countries hit \$31 billion last year (chart). **NONSTOP SERVICE.** A big step toward expanding trade will be the open-skies accord. It would replace a 1966 pact that is so restrictive that almost two-thirds of the 100 largest U.S. cities don't enjoy nonstop air service to Canadian cities. The

current pact doesn't even allow nonstop flights between Ottawa and Washington. By one estimate, the number of passengers on scheduled flights between the two nations would more than double, to 19 million a year, after the three-year phase-in period.

With relations so cordial, Canada will argue during the Clinton visit for eliminating antidumping suits from NAFTA. After all, with the U.S. and Canadian economies integrated as never before, it makes about as much sense to charge Canadian goods with dumping in the U.S. as it would to charge Ohio companies with dumping in Pennsylvania.

By William C. Sullivan
Months in Ottawa, with bureau reports

CROSS-BORDER INVESTMENT JUMPS



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REPUBLICANS MAY HURT TAIWAN BY TRYING TO DO IT FAVORS

As if a threatened trade war and squabbles over human rights and missile trafficking weren't causing enough trouble in U.S.-China relations, a new flashpoint is about to ignite. Congressional Republicans and some Democrats are pressing President Clinton for warmer ties with Taiwan, the island of 21 million off China's coast that Beijing considers a renegade province. Taiwan has suffered near-parity status in Washington since 1979, when the U.S. officially recognized Beijing as the only legitimate Chinese government. But now, GOP leaders think it's time to reward Taipei for progress it has made toward democracy. Taiwanese President Lee Teng-hui's desire to visit his alma mater, Cornell University, this spring presents the perfect opportunity. While Clinton marginalized curbs on Taiwan last fall, he specifically reiterated a longstanding U.S. ban on visits by Taiwan's president. Republicans say that unless Clinton lets Lee visit Lake Cayuga's shores, they'll write immigration laws or the Taiwan Relations Act to override him.

MILITARY ACTION? Clinton has probably put himself up for yet another embarrassing foreign policy flip-flop. But more than the President's ready-made low prestige is at stake. China would see a Lee visit as violating an explicit promise," says Harry Harding, a China scholar at George Washington University. Even so, Beijing might hold its ire in check. But if Republicans push so far and whip up Taiwan's independence movement, that might provoke military action by China's leaders, who are on edge as Deng Xiaoping fades from the scene. China has never renounced the use of force against Taiwan if the island formally proclaims its independence. So instead of doing Taiwan a favor, GOP hard-liners would be jeopardizing its prosperity and the region's stability.

A big tilt toward Taiwan could also halt what appears to be

a recent softening of Beijing's usually tough tone toward Taipei. In a Chinese New Year's speech, President Jiang Zemin raised the possibility of visiting Taiwan and emphasized the need for peaceful reunification.

So Washington's tough task is to improve relations with Taipei without going over the line. The U.S. is caught in a tug-of-war between Beijing and Taipei. Taiwan's ruling party is being pressed by the pro-independence Democratic Progressive Party. With Taiwan presidential elections looming in early 1996, Lee needs to show he's boosting the island's international standing. His government is underwriting a lavish lobbying campaign in Washington to drum up support for his visit as well as Taiwanese membership in the U.N. American business, eyeing juicy infrastructure contracts in Taiwan, also wants diplomatic concessions.

The Administration would prefer to try to accommodate Taipei's ambitions through less controversial measures such as pushing for Taiwan's membership in the World Bank. The hope is that mainland China and the Taiwanese will achieve some sort of mutual acceptance. Already, trade between the two countries is booming to the point that Taiwan has proposed dropping its ban on direct shipments to China. Taiwan's China Airlines is mulling removing the national flag from its planes in anticipation of eventual direct flights to the mainland. "The economic imperatives are so strong that they are likely to find a way" to get along "unless someone makes a stupid mistake," says John S. Wadsworth Jr., chairman of Morgan Stanley Asia Ltd. But with congressional Republicans turning up the heat, the risk is that such tentative moves toward accommodation could go up in smoke.

By Amy Borrus in Washington, with Margaret Dawson in Taipei



CLOUT: Will Taipei provoke Beijing?

GLOBAL WRAPUP

WARBURG AGAINST THE WALL

Sir David Scholey, acting CEO of J. G. Warburg Group PLC, faces an unenviable task as he tries to pull Britain's leading investment bank out of its nosedive. Scholey, who took over after the resignation of the Earl Cairns, must either prune Warburg away back or search for a partner that would provide the kind of clout it hoped to get from its failed merger with Morgan Stanley Group Inc.

Retrenchment will further bruise Warburg's morale, but that is the course Scholey

seems to be steering. Scholey may trim or dump such operations as its U.S. trading and research unit or its European securities distribution arm. Scholey denies he's retrenching: "We will continue to build the business, though on a smaller scale than if the Morgan deal had been completed."

Merging may be a better plan. While Scholey denies he's talking to other potential partners, suitors are circling, including Germany's Dresdner Bank. And American players without a big European presence could be interested.

Scholey faces a tough balancing act: cutting costs without triggering more defections. In early February, Warburg lost its co-heads of equity capital markets to Deutsche Bank's Morgan Grenfell Group PLC. Uncertainty over bonus levels, possible layoffs, and division cuts could accelerate the departures and reduce the price the bank could get for itself. Yet if Scholey doesn't slash away enough, profits will continue to drop. That's why many analysts doubt Warburg can stay independent for long.

By Julia Flynn in London

THESE ADS HAVE WINDOWS AND WALLS

Flagship stores for brand names are booming

The new OshKosh B'Gosh Inc. store on Manhattan's Fifth Avenue has plenty of the tyke-size blue-and-white-striped overalls the company is famous for. But it also has lavish displays of OshKosh shoes, underwear, and even toy bears, items you're not likely to find in even the largest department stores.

And that's the idea. OshKosh is just one of a raft of manufacturers that are opening their own flagship stores. Powerhouse brands such as Nike, Speedo, and Levi's, widely carried by retailers large and small, now have entire stores devoted to their labels. Department and specialty stores typically carry just 60% of a line—and sometimes much less—but these captive stores have it all.

Why this new breed of company store? The consolidation of department-store chains has left manufacturers with fewer stores to sell to. And profit-starved retailers have been pushing their own competing private-label brands. Above all, though, these new stores are a kind of life-size, interactive ad, meant to boost brand awareness for the makers of everything from apparel to electronics. "For manufacturers, it used to be 'should I open a retail store?' Now, it's 'how many should I open?'" says Kate A. Murphy, a retail consultant with Fitch Inc., an Ohio-based business consultancy.

THEATRICALS. The single-label stores give consumers a chance to see the entire line arrayed the way the designers intended. Although most make a little money and a few are solidly profitable, the goal here is marketing and old-fashioned brand-building, not establishing a new profit center. "It's a showcase store," says Paul Lowry, vice-president for retailing at OshKosh. "We expect it will make a profit, but that was not the object."

The idea isn't completely new. Clothing designers have long operated image-building shops

on Manhattan's Madison Avenue, and Sony Corp. opened a Chicago store in 1991. But the captive stores are now spreading quickly (table). Most are glitzy, theatrical showcases designed to play off of a brand's image. The New York OshKosh store features a giant wooden train station meant to evoke the brand's roots in making overalls for engineers. Nathalie Berger, visiting from Paris, stopped in the store recently as she strolled down Fifth Avenue. "It's wonderful, very different from Paris," she says.

Nike Inc. has sprinted full speed ahead with Nike Town, now in four U.S. locations, including a 68,000-square-foot behemoth in Chicago. Part high-tech sports museum, part fitness theme park, the Chicago store includes a basketball court and video theater. Nike cares more that visitors to Nike Town carry away fond memories of the brand than a new pair of sneakers.

Authentic Fitness Corp.'s Speedo stores sport mannequins that appear to be diving from swimming-pool-tiled ceilings. The 48 Speedo stores average sales of \$450 a square foot, above management's initial target of \$425. "We're in business to make money," says Linda J. Wachner, the chief executive of Warnaco Inc. who also heads Authentic. "But this is also the best advertising we can have."

The target of that advertising is the consumer, of course, but it's also the retailer. Manufacturers figure that if the flagship stores boost brand awareness, retailers will

give more space to their wares. The stores also give them a way to stay in direct touch with customers. Based on requests from store customers, for example, OshKosh may revive the little girl sizes that it dropped a few years ago after its retailers insisted that shoppers thought of OshKosh as only for toddlers.

Big retailers seem resigned to the competition so far. Levi Strauss opened a 6,000-square-foot Original Levi's Store directly across the street from Bloomingdale's in Manhattan, but Bloomie's says the store attracts a different kind of shopper and has had no impact on its sales. Another thing that helps pacify retailers: The flagships sell at full list price—no end-of-season sales and no markdowns.

Flagship stores are just one of the channels manufacturers are experimenting with to sell goods directly to their consumers. Whether they ring up more in sales than home-shopping TV shows or online shopping services may not matter as long as they make a strong impression. If the 1980s gave us stores as theater, the 1990s have given us stores as infomercial.

By Mary Kuntz in New York



WHAT A DIVE: At Speedo, some dummies are overhead

BRAND-NAME SHOWCASES

STORE NAME	NO. OF STORES
Speedo Authentic Fitness Stores	48
Original Levi's Stores & Dockers Shops	16
Nike Town	4
OshKosh B'Gosh	3
Reebok Concept Stores	3

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By now, the vision of our future in cyberspace is pretty familiar. From Al Gore and Newt Gingrich to Bill Gates and John Malone, dozens of academics, business leaders, and politicians have painted a detailed picture of the coming digital millennium. We'll work, shop, chat, educate, and amuse ourselves in a new online realm that will put every conceivable form of information—from a stock report to a digitized, interactive movie—instantly at our fingertips. Already, millions of people who collaborate across

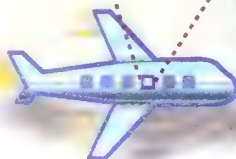
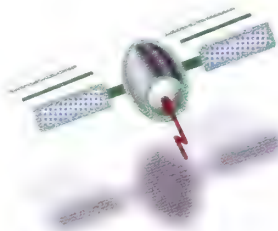
computer networks or log on to commercial online services prowl the vast Internet are seeing a glimmer of how the vision will come to life.

They're probably seeing something else as well: Despite the high-speed networks and powerful PCs to take you there, cyberspace—especially the uncharted expanse known as the Internet—is still not a safe, hospitable, and compelling environment for businesses and consumers. Often, it seems a harsh and unforgiving place where, with a misplaced keystroke,



USER INTERFACES

Browsers and navigational aids will help sift through the sea of information, helping you find what you are looking for, whether from a PC, a wireless device, or your TV. Software "agents," sort of personal assistants, will go out on the Net and fetch stock quotes or the best deal on airfares to Hawaii.



COMPRESSION

Until networks get more powerful, compression techniques are vital for squeezing hefty video, graphics, and text files for faster transmission over the Net.



SECURITY

Encryption technology scrambles digital signals to help keep confidential data, such as credit-card numbers, from cybersnoops.



Cashing in on Cyberspace

A Rush of Software Development

can become hopelessly lost, where the information you might find isn't where it should be, and where it's too easy for villains to snatch your digital valuables—by buying off your work or stealing your credit-card information. What will change all that? In a word: software. There is an enormous need for “enabling” software—to speed up transmission of huge video files, to guide you through hundreds of TV channels, to manage thousands of online transactions, and to make sure those transactions are secure. “The solution to everything on the Internet is software,” says Edward J. Hooper, senior vice-president at MasterCard International Inc., which expects its member banks to start doing business on the Net this year. “Software is king.”

THE LAND RUSH. The great cyberspace software race has begun. At giant corporations and in basements, the brightest minds in software are working on programs that will make it possible to move vast amounts of digital information, distribute it efficiently to the correct addresses, and make it all simple enough for nontechnies to manage. From simple graphical interfaces to such cutting-edge concepts as software agents, programmers are harnessing the power of cyberspace—to help businesses and consumers meet in an electronic marketplace and to create the information systems for the virtual corporations—and communities—of the 21st century.

The players that come up with these programs could wind

MULTIMEDIA SERVERS

Some companies are betting that entertainment will create a mass consumer market in cyberspace. Applications such as movies on demand and interactive games will require powerful multimedia servers.



PUBLISHING PROGRAMS

Publishers looking to move their digitized content to the Net need tools to help them create and maintain compelling outposts in cyberspace.



ONLINE SYSTEMS

Some sorts of companies are beginning to hawk their wares in cyberspace, setting up electronic malls and storefronts.



ELECTRONIC COMMERCE

Banks and software companies see electronic banking as a big consumer market. To attract businesses to the Net, they are working on a range of projects to make networks secure.



Create an Electronic Marketplace

up at the head of a new world order—where computing, entertainment, and communications merge. “It’s like the land rush in Oklahoma,” says Lawrence J. Ellison, chairman of Oracle Corp., the No. 2 software maker. “The best spot in the valley goes to the one who gets there first.” Ellison, who has launched ambitious efforts to develop software for everything from serving up video on demand to home shopping and information searching, is determined to get there before No. 1

Special Report

Microsoft Corp. And Microsoft Chairman William H. Gates III is just as determined to extend his software reign into the Information Superhighway era. Microsoft is spending more than \$150 million a year on developing all sorts of software for entertainment and information networks.

Or neither could prevail. The battle for cyberspace presents a fresh opportunity—for startups as well as for some of high tech’s most venerable names. Both IBM and Digital Equipment Corp., for example, are scrambling to redeploy their software expertise for the I-way. “Software tools that collect information, organize it, and make it readily available will be perhaps one of the biggest businesses on the Information Superhighway,” says William D. Strecker, vice-president of Digital’s Advanced Technology group.

Lotus Development Corp., whose Notes program is now used by corporations to coordinate the activities of workers across a network, is also well positioned to help Corporate America move into cyberspace. The company is already working with AT&T on Network Notes, which will run on the phone giant’s long-distance system, and developing connections between Notes and the Internet. “It’s a period of dramatic change and innovation,” says Erik Grimmelmann, marketing vice-president for business multimedia infrastructure at AT&T. “Inevitably, some of those on top will fall.”

USER-FRIENDLY FACADE. The first leg of the race is well under way. It’s the effort to create the kind of “user interface” that will bring millions of ordinary people into cyberspace. This ranges from programs for your desktop computer that simplify connections to your corporate electronic-mail system to software to whisk you across the Net to shop in virtual malls, visit cybershowrooms, and ring up bills at the electronic newsstand. Already, software makeovers of America Online Inc., on which BUSINESS WEEK is electronically available, and Prodigy Services Co. have converted those commercial services into a relatively user-friendly, if limited, window into cyberspace.

The most critical need, however, is to create a facade of user-friendly software for the globe-spanning Internet. A jumble of interlinked networks, the Internet includes some 4 million “server” computers, housing incalculable volumes of all sorts of information. But because there is no central control over the Net, there is also no master index. That has kept the Net largely a playground for the techno-intelligentsia who use arcane programs such as Gopher, Archie, and FTP to dig out what’s hidden in all those databases.

Now, the software is emerging that will make it possible for ordinary consumers and businesspeople to do the same—making the Internet the all-purpose route into cyberspace. The big breakthrough began in 1993 with the creation of an Internet subnetwork called the World Wide Web—really just a clever software scheme for imposing order over the mass of free-form information on the Net by organizing it in easily understood “pages.”

What makes the Web such a powerful cyberhelper is a software technique known as hyperlinking. When composing a Web page, an author can create hyperlinks—words that appear

in bold type and indicate a shortcut to some other information. Using a program known as a Web browser on your PC, you can read pages stored on any Web computer. Say you're reading a page that describes recent discoveries about allergies. You

see the word "antigen" in bold type. Using your computer mouse, you click on the word

Special Report

and—without any further effort on your part—you are transferred to another Web page that tells you what an antigen is. That page could be in the system where the first page was or in another computer thousands of miles away.

THE SURGE IN BROWSERS. The Web is emerging as the laboratory for learning how to do business in cyberspace. Companies of all stripes are experimenting. Club Mediterranée has Web pages describing its resorts. IBM has posted its annual report. And on Feb. 14, Fidelity Investments launched a "home page" with descriptions of its funds, a worksheet for college planning, and a sample of its personal-finance software that Internauts can download. Log on to the Web computer of Philadelphia-based CDnow! and you can order from its online catalog. Click on an album title, and see the names of the songs. Another hyperlink will get you to reviews. With a click of the mouse, you can toss an album into your "shopping cart." When you're done, you order by sending your credit-card number over the Net.

As Web use has exploded—there are now 27,000 Web sites, and the population is doubling every 53 days, according to Sun Microsystems Inc.—Web browsers have become an overnight software sensation. Millions of copies of Mosaic, the original Web browser, have been distributed for free over the Net. Still, companies are piling into the browser business—often with up-

grades of Mosaic. Spry Inc., a Seattle-based startup, sells Internet-In-A-Box. Quarterdeck Office Systems Inc., a PC software maker looking for new life, sells a series of Web products and startup Netscape Inc. offers Netscape Navigator, written by Mosaic creator Mark Andreessen. At the same time, browsers, ranging from Prodigy and America Online to Microsoft and Novell, are building Web browsing into their software.

The Internet is not the only focus of the software race. Virtually all major computer and software makers are working on interface programs to help office workers move smoothly from their desktops to corporate networks and beyond. One approach is the "universal browser," intended to mask the boundaries between various computers and networks. Instead of having to figure out where the information is buried—and then trying to somehow connect with the right system—computer user will simply specify what kind of information is needed. "Where it comes from, how it got there, will recede into the background," says AT&T's Grimmelmann.

Novell Inc., the leading supplier of software to run local-area networks, is testing a universal browser code-named Corsair. It uses cartoon-like pictures to help you get your bearings. For example, a screen depicting an office shows a desk, Rolodex, phone, mailbox, and file cabinets. When you're going beyond your own organization, you click on the office window and are transported to a screen with a colorful picture of the world outside your virtual window: a leafy village with a shopping center, a city hall, a bank, and a business park. Clicking on the business park might call up a yellow-pages listing that displays information services you can connect to.

Similar programs are under development across the computer industry. IBM is working on one for its OS/2 operating system, and Computer Associates International Inc. is putting

WHAT'S THE COLOR OF CYBERMONEY?

Doing business in cyberspace sounds like a great deal—low overhead, no real estate, no traffic. But how are you going to get paid? Or pay for what you buy?

Electronic payment systems are among the most challenging issues facing programmers. It's relatively simple to create digital equivalents of checking and credit-card accounts—and to protect them with encryption—but that's only part of the answer. Electronic replicas of those account systems won't be well suited to making "micropayments" for snippets of information that will be bought and sold on the Internet.

And there's another issue. When consumers start doing business across the untamed Internet, they will vastly increase the chances that confidential data about them can be compiled. Those risks exist now, but on the Net, every transaction leaves a trail—that a hacker, an aggressive marketer, or the government could pick up. And it's more than Internet purchases: credit-card issuers are plan-

ning "smart" cards for use with everything from pay phones to public transit. "The potential for invasion of privacy becomes severe," says Don Tapscott, director of the Alliance for Converging Technologies, a private research outfit.

One answer is to create the electronic equivalent of cash—digital money

that can be loaded onto your hard drive or a wallet card and used as freely and anonymously—as cash. That's the idea behind First Virtual Holdings, which runs a kind of private currency system on the Net, and DigiCash, a Dutch software startup.

DigiCash's "ecash," now being tes-

A CONTENDER
Ecash, developed by Chaum, is being tested on the Net





PERSONAL COMPUTERS Software

makers are creating graphical user interfaces that make it easy to tap into a network—whether it's your corporate database, an E-mail system, or the Internet. Novell's Corsair program mimics a real-world landscape. A built-in searching program called Ferret retrieves information for you.

finishing touches on a package called CA-Simply Village. In addition to three-dimensional graphics of familiar images, Simply Village has speaking cartoon characters to help guide through using a variety of consumer services. Microsoft's approach is embodied in Windows 95, the new Microsoft operating system due out this August. It has built-in links to the Internet and to the forthcoming Microsoft work, an online service. In addition, it's organized to help workers move seamlessly between files on a PC and

those on a local-area network or on a computer on the other side of the ocean—all through a series of screen icons. Windows 95 also includes a technology called Object Linking & Embedding (OLE), which is similar to hyperlinking.

So far, the hottest startup in the cybersoftware race is General Magic Inc. Its initial public offering came out at \$14 on Feb. 10 and traded as high as \$34 that day—despite five years of losses and scant revenue. What has investors so excited is a pair of products that could greatly simplify getting

Internet, is the brainchild of founder David Chaum, a computer-science professor at the University of California at Berkeley. Earlier electronic payment systems, protected with encryption technology. With a credit-card or electronic payment system, encryption stops snoopers from getting your account numbers from the merchants and card issuers purchasing information.

With ecash, the encryption not only protects the money from snoopers and thieves but also obscures the identity of the owner. Here's how: When you want cash, you make an electronic withdrawal from your bank account. The bank issues electronic currency—a series of encrypted serial numbers representing dollar bills and coins. Once the encrypted money leaves your account, it can no longer be traced back to you—not even by the issuing bank. When you spend it, your digital coins get deposited directly to the merchant's ecash account.

NERVOUS BANKERS. While ecash can't guarantee your privacy—merchants can still keep track of where they send their wares—it does play an important role in making the I-way a better place to do business. With a digital cash system in place, anyone with a computer and a modem could peddle their ideas or wares on the Net—whether a short story, a work of digital art, or investment advice.

Not everyone is cheering. Banks, credit-card issuers, and the Internal Revenue Service are less than eager to see untraceable digital money catch on. "We are the antithesis of anonymous cash," says Richard M. Loneragan, senior vice-president for point of transac-

tion at Visa International. The credit-card giant is working with Microsoft Corp. on a secure electronic credit-card setup for the Net.

Banks could be the biggest losers. In the ecash pilot, DigiCash acts as its own bank—but it is just playing with digital Monopoly money for now. Even though Chaum hopes to work with leading banks, there's really no need to. And that has some bankers alarmed. "We have to ensure that we own a piece of every transaction, whether it's a movement of funds or information," says Charles H. S. Mallis, global marketing executive for global payments and treasury services for Chase Manhattan.

In the end, there will likely be multiple payment methods in cyberspace, just as in the real world. Microsoft, for example, has a credit-card venture with Visa but is quietly looking into electronic money, too. And Wells Fargo & Co. is looking into electronic cash. "It's fairly clear that there has to be action on the part of banks," says Maria Mandler, senior product director at Citibank global cash-management services, "or I'm sure other organizations will fill the gap." With digital cash, perhaps.

By Amy Cortese, with Kelley Holland, in New York

Companies on the Trail of Electronic Money

CASH Working with Wells Fargo on a system to encrypt credit-card data

DIGI Wants to create the digital equivalent of cash—totally anonymous and universally accepted

VIRTUAL HOLDINGS Has launched a digital cash system for small transactions

NET Developing a specification for credit-card transactions with Visa

ECASH This British banking venture is developing a smart card system for electronic cash

SECURE Building encryption and validating its Web software with MasterCard, Bank of America, MCI

around in the online world. Magic Cap, designed initially for use on handheld gadgets, uses a series of metaphorical scenes: your office, the hallway outside, and a downtown. By simply pressing on the icon representing an out box, you can send a

memo to a dozen co-workers on a mailing list via a wireless data network. Magic Cap is

Special Report

being used by Motorola Inc. and Sony Corp. in their personal digital assistants.

But it's General Magic's other product, Telescript, that really shows promise. A software language for creating applications on a network, Telescript includes a new technology called software agents. Agents can act on their own to get something done for you. So, for example, an agent could be programmed to automatically scour the Net for the best deal on, say, a 30-year fixed mortgage—and order up an application form. The first Telescript application will be PersonaLink, an "intelligent" messaging service being launched by General Magic backer AT&T. While AT&T says the system will eventually handle such tasks as doing your online shopping, at first the agents will do simpler chores, such as routing E-mail messages.

"NOT FOR THE FAINT OF HEART." For now, creating electronic shopping assistants isn't a top priority. What's needed first is software to keep people from drowning as they sift through a sea of information to find exactly what they want. Every day, that sea grows deeper: There are now some 5 million documents stored on Web servers, estimates Michael Mauldin, a research computer scientist at Carnegie Mellon University. That figure is doubling every six months to a year, he figures.

At Carnegie Mellon, Mauldin and his team have created what he calls a software "robot." Running simultaneously across four powerful workstations, the system is called Lycos, after the Lycosidae spider, known for pursuing its prey relentlessly. Lycos goes out onto the Web and catalogs the continually expanding number of documents posted there by scanning them and creating an abstract containing the title, first 20 lines of text, and the 100 most important words. Since beginning its mission last June, Lycos has cataloged 270,000 documents—a mere 5% of what's on the Net. Mauldin says it will take 12 computers running Lycos to keep pace with the growth of Internet information.

Oracle, the top supplier of database programs for minicomputers, is also working on ways for ordinary folk to find needles in digital haystacks. Last fall, it announced plans to adapt a "natural language" search program called Context for



INTERACTIVE TV Trials are beginning in earnest this year. Oracle's I-TV software offers services such as home shopping.

the Internet. Using simple English—rather than stilted computerese—you can ask Context to search the entire Net for specific information.

Context is only a tiny part of Oracle's I-way effort. Its primary target is the software to run video "servers"—powerful computers with massive arrays of disk drives that can run interactive-TV shopping channels or dish out video on demand across cable-TV or phone networks. So far, the company has contracts with British Telecom, Bell Atlantic, and Time Warner to build servers for interactive-TV trials. At the other end of the line, Ellison is looking at interface software: One reason he has considered mounting a takeover of Apple Computer Inc. say Ellison associates, is that he believes Macintosh software could be the basis for an I-way interface—for computers and cable-TV set-top boxes.

Ellison is also pushing his company into the business of selling software that will create digital content. The first program, Media Objects, is now in prerelease testing. Another



HANDHELDS A new crop of handheld computers and personal communicators will connect you to the Net through wireless transmission. General Magic's software "environment" gives users a simple interface through which to pull down stock quotes or fire off E-mail on the go.



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project, the World Wide Web Kit, is aimed at helping current customers link their Oracle databases to Web pages.

Although it got a later start, Microsoft is attempting to match virtually every Oracle move in I-way software. While

Oracle has snagged the biggest phone contracts, Microsoft has lined up cable giant

Special Report

Tele-Communications Inc. and Rogers Cable in Canada. TCI plans to use Tiger, a Microsoft video-server program, to provide movies on demand. Microsoft is also developing channel-surfing software for set-top boxes and software "tools" to help businesses create content for the Microsoft Network.

The high-stakes contest to build software for interactive TV has attracted other players as well. Hewlett-Packard, DEC, Silicon Graphics, Sun, IBM, and Sybase are all betting chunks of their research and development budgets. "The race is going to be won by those people who have guts and are willing to spend money now," says Andrew T. Eiseman, head of technology for U S West Communications Broadband & Multimedia Services, which is testing a DEC server and set-top boxes from game maker 3DO Co. "This is not for the faint of heart."

While the big guys slug it out in interfaces, information retrieval, and video-server programs, there are lots of niches for others. Take eShop, a four-year-old San Mateo (Calif.) startup. It has come up with three programs to help merchants set up their own distinctive virtual stores. One creates an electronic storefront. Another is a "warehouse" package that manages product and customer information and routes transactions. And the third is a browser for electronic catalogs—whether they're on the Web or on interactive TV. eShop plans to take a cut of the revenues from retailers and has licensed its software to AT&T, which is developing a shopping service for its PersonaLink service. Another client is Tower Records, which is testing an electronic shopping system.

PERSONAL NEWS. Software to help publishers go online is another thriving niche. One of the leaders in electronic publishing software is WAIS (Wide Area Information Servers). Its WAISserver system will handle billing, registration, advertising tracking, and just about anything else a publisher needs. WAIS also offers intelligent-agent and information-searching software, which WAIS president Brewster Kahle helped develop at supercomputer maker Thinking Machines Corp. Customers include Dow Jones & Co., which is testing an electronic version of *The Wall Street Journal* that lets subscribers specify what news they want to get—by selecting company names and sections of the regular paper. "This is the start of the personal news service," says Kahle.

Before publishers—or anybody else—start doing a lot of business in cyberspace, there's another software issue to deal with. How do you make sure information used in electronic transactions can't be tampered with? How can a seller be sure a virtual customer is who he claims to be? And what con-

sumer wants to trust the network with a credit-card number?

Partly because there have been few answers, business volume across the Net has been modest. Roughly \$200 million worth of credit-card transactions took place over the Internet last year—barely a drop in the bucket: Visa alone rang up \$64 billion in charges in 1994. And most Internet purchases were offline—the buyer browsed the Net then ordered by phone. For good reason: "Passing your credit-card number over the Internet today is like getting dressed with the light on when it's dark outside," says Richard K. Crone, a senior manager at KPMG Peat Marwick's financial-services consulting practice. That's holding back electronic commerce in general, says Richard M. Lonergan, senior vice-president for point of transaction at Visa International.

Recent security breaches on the Internet have done nothing to help. "This could potentially be a fantasy for hackers worldwide," says Joel Friedman, a specialist in banks and

credit cards at Andersen Consulting. And the efficiency of the Net increases the potential damage: a cybersnoop could fire off dozens—even hundreds—of phony transactions in just a few minutes. "Consumers are hearing it's insecure, so stay away from it," says MasterCard's Hogan. "We have to go through a PR effort to undo that."

SECURITY TEST. Software companies, banks, and researchers may have the solution in hand. There are at least a dozen initiatives under way (page 80). Microsoft is working on several secure payment systems, including one with Visa for credit-card transactions. Netscape has built encryption into its browser and Web-server software. CyberCash, a Vienna (Va.) startup, is working with banks such as Wells Fargo & Co. on electronic payment systems.

Many of these systems will be tested this year. Wells Fargo Bank, for example, plans to start a secure credit-card pilot next month with 10 to 20 merchants. The system will go "live" in April, available to any merchant doing business with Wells. The bank also plans to offer debit cards on the Net. MasterCard says it will test a secure credit-card service on the

Net by midyear and hopes to offer it commercially by fall. Visa and Microsoft, meanwhile, plan to have a payment system in place by yearend. And DigiCash, a Dutch startup, is working on something called ecash, a sort of digital currency that will be useful for small-scale purchases—from 5¢ to \$5—on the Net.

Whether it's digital cash, debit cards, or credit cards, the new electronic payment systems all will be secured by some form of encryption—software algorithms that scramble digital bits of information so they cannot be read by unauthorized eyes. The most promising form is the "public-key" method and the most popular public-key system is being licensed by RSA Data Security Inc. (page 86).

One by one, as I-way software issues are tackled, the I-way software business could disappear. How? All the various programs needed to create, move, and view digital "content" will be built into other software. That's already happening with HTML (hypertext markup language), the software forma-



ONLINE SERVICES Prodigy is the first of the major commercial online services to offer full access to the World Wide Web. Subscribers can view Web "pages" through Prodigy's browser.

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used to create Web pages. The leading makers of word processing programs—Microsoft and WordPerfect Corp., a division of Novell—have announced plans to add HTML to their packages. And Lotus' new InterNotes Net Publisher converts Notes documents to the Web format. Even IBM is reworking its main-

Special Report

frame database, DB2. The new DB2 World Wide Web will provide access to corporate data from the Internet.

In fact, one measure of the success of the cybersoftware ef-

fort will be how quickly the new programs seem to vanish. If businesses are to operate efficiently online and consumers are to enjoy their time in cyberspace, the programming that makes it all possible must be invisible. Only then will those visions of life in cyberspace come true.

By Amy Cortese, with John Verity, in New York, Russell Mitchell and Richard Brandt in San Francisco, and bureau reports

America Online users can chat with the authors on Sunday, Feb. 19, at 9 p.m. EST in a BUSINESS WEEK Online conference

THE KEY TO SAFE BUSINESS ON THE NET

They came from AT&T. Oracle. National Semiconductor. Adobe Systems. Visa International. Speaker after speaker, more than 20 in all, crowded about tiny RSA Data Security Inc.'s products at a conference hosted by the company. "Gee," said a friend who whispered into RSA President Jim Bidzos' ear. "You must have pictures of all these guys with hookers, naked."

Well, no. What RSA has is something really useful—software to

and less than \$10 million in sales. But with computer and online companies and giants such as Visa International and MasterCard International Inc. using RSA technology, the company is poised to take off. How big? "It'll be a nuclear explosion," says Bidzos. He figures revenues will double each year.

The fuel is a rather simple concept. Each party in a transaction holds two software "keys." Public keys are published, like listed phone

So far, nobody has cracked the code, despite an annual RSA hackers contest. RSA figures it would take a supercomputer hundreds of hours to get just one credit-card number. The biggest risk, then, is sloppy protection of a private key.

SIGNING UP LOTUS. RSA's success comes almost in spite of itself. Its technique was invented by Stanford University researchers in 1977. Three Massachusetts Institute of Technology professors—Ronald L. Rivest, Adi

Shamir, and Leonard M. Adleman—made it a usable system, then founded RSA and nailed down crucial patents. But, says Adleman, now a professor at the University of Southern California, his "lack of aptitude in business" almost sank the company. Rivest, the chairman, is the only founder still active in RSA business.

When Bidzos, a marketing expert, arrived in 1986, the company "was \$750,000 in debt and had no customers," he says. That year, RSA signed up Lotus Development Corp., which uses the technology in Notes. Since then, the client

list has swollen. The latest: AT&T and VLSI Technology Inc., which will use RSA algorithms in encryption chips.

Will the love-in last? RSA's main patent expires in five years, and Viascrypt, a tiny company that licenses RSA technology, is mounting a challenge—but with little success thus far. A big factor in RSA's favor: Although it's in a position to do so, it is not gouging on price. "They have not been piggy," says Edward J. Hogan, senior vice-president at MasterCard. Even now, says Bidzos, "I don't see us raising prices." That's how to win friends and influence people.

By Russell Mitchell in Redwood City, Calif.



make doing business in cyberspace safe. Outside of spy agencies, RSA's "public-key encryption" is regarded as the best security there is. Ask RSA's big-name clients—Apple, Microsoft, Motorola, and Lotus. "Public-key cryptography is a cornerstone of the Information Superhighway," says Nathan P. Myhrvold, Microsoft Corp.'s senior vice-president for advanced technology. "And RSA is the most widely accepted public-key system." Acceptance didn't come overnight. The privately held Redwood City company took 12 years to reach its current size: 45 employees

DIGITAL LOCK Bidzos challenges hackers to crack RSA's code—but so far no one has

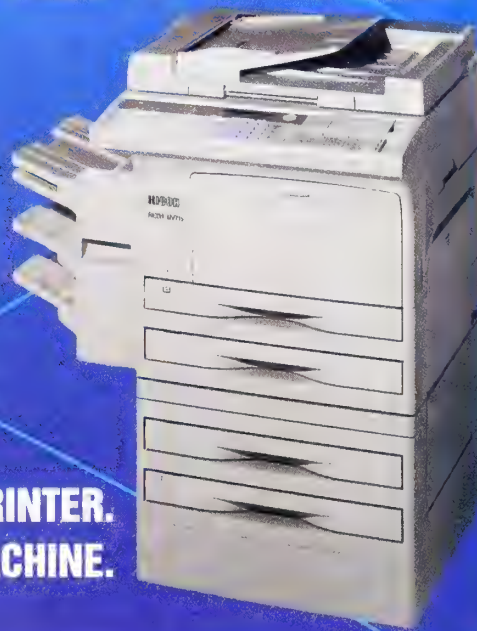
numbers. Private keys are known only to their holders. Both keys are needed to encode and decode a message.

Example: To buy flowers on the Internet, you encode your credit-card

number using the public key of the card issuer. The only key that unscrambles the data to complete the transaction is the issuer's private key. Or you send E-mail coded with your private key and the receiver uses your public key to decode it. Since the public key unlocks only messages that were encoded with your private key, the receiver can be sure you're the sender.



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WHAT DID RON BROWN KNOW, AND WHEN DID HE KNOW IT?

New evidence links him to efforts to secure controversial oil deals while at the DNC

Ronald H. Brown is nothing if not consistent. As congressional and Justice Dept. investigations probe deeper into the Commerce Secretary's past business dealings at First International Communications Corp., Brown has insisted he was merely a silent partner at the Washington-based consulting firm. Even when it was revealed that he received \$400,000 for his share in First International in 1993-94 though he never invested a dime in the company, Brown has maintained that he was oblivious to the company's dealings.

But sources familiar with First International's activities and documents obtained by BUSINESS WEEK appear to contradict Brown's assertion that he was a distant, hands-off partner in the firm. The documents, including internal First International memos, show that Brown was kept informed of at least two separate pending deals while serving as chairman of the Democratic National Committee and was sometimes an active participant. In one memo, dated Apr. 29, 1992, Nolanda Hill, Brown's business partner at First International, refers to correspondence between Brown and Angelan contacts about a plan to buy oil at a discount price and exhorts him to move quickly on the deal "as the ball is in your court as far as [he] is concerned."

Two months later,



SILENT PARTNER
Brown denies any wrongdoing and calls the uproar a GOP "smear campaign"

a memorandum to Hill and copied to Brown, Fernando Pegado, a London middleman, outlined a deal to buy crude from Aramco, the Saudi state oil company. With a proposed \$1.70-a-barrel discount, the deal could have fetched a profit of \$2.5 million a year for Brown and Hill, based on market prices. Pegado is the husband of Lauri Fitz-Pegado. At the time, Fitz-Pegado, a longtime Brown associate, was a public relations executive. Now, she promotes overseas business development as head of the

Commerce Dept.'s U.S. Foreign & Commercial Service. Through her attorney, Fitz-Pegado says she played no part in any oil deals involving Brown, and there is no evidence to suggest that she did. **"ALL TALK."** Although both deals ultimately fell through and there is no suggestion that Brown did anything illegal, his pursuit of oil deals first as a prominent party figure and later while serving as Bill Clinton's nominating-convention manager are bound to heighten the debate about whether Brown was trying to profit from his rising political stature before he became Commerce Secretary in 1993. London oil traders who regularly do business with Aramco say the terms mentioned in the memos were so potentially lucrative that Brown and Hill may have been targets of a scam. But Steve Stylianoudis, a Washington defense contractor who worked for the Saudi royal family for five years, says such discount deals for influential politicians are a common practice among Arab oil states.

Through his attorney, Reid H. Weingarten, Brown denies any wrongdoing. "Yes, he tried to get involved in oil transactions in Angola," Weingarten acknowledges. "But he was never successful in doing so, and he has never advanced any private interests in his official capacity as Commerce Secretary. As for the Saudi deal, Weingarten says Brown

BROWN'S ADVENTURES IN OIL

Ron Brown has maintained that he was unaware of the business dealings of First International, the consulting firm he co-founded with Nolanda Hill. But he was kept apprised of at least two abortive deals during his tenure as DNC chairman:

APR. 29, 1992 In a memo to Brown, Hill outlines a plan to buy Angolan oil. She urges Brown to act quickly on the proposed deal, "as the ball is in your court." The deal is ultimately rejected by SONANGOL, Angola's national oil company.

JUNE 26, 1992 Fernando Pegado outlines a plan to buy Saudi crude from Aramco. In a memo to Hill, copied to Brown, he proposes an oil deal that could have produced annual profits of \$2.5 million for Brown and Hill. It is never consummated.

is unaware of the plan and that Hill rsued it on her own. "It was all talk," ys Weingarten. "Everybody was talking, and nobody was close to any oil." ill, through her attorney, declined to mment.

Brown and Hill founded First International in 1990. Hill, a major Democratic donor, was running Corridor roadcasting Corp., which owned TV ations in Needham, Mass., and Washington. First International, which operated out of Corridor's offices, appears ver to have made a successful investment. Yet despite its seeming lack of ecess, First International appeared Brown's 1993 financial disclosure report as his single largest asset—worth 600,000 to \$1 million.

At various times, First International ied unsuccessfully to import alcohol and Beatles posters from Eastern Europe. Then, in the spring of 1992, Brown approached SONANGOL, the Angolan state oil company, through

the company's ongoing "Angolan Oil Project." She revealed to him that she had lined up the services of FFP Partners, an oil consulting firm in her home state of Texas, to negotiate the sale and delivery of crude. Attorneys for FFP declined to comment. In the end, SONANGOL rebuffed Brown's overtures to buy oil at discount prices, sources close to the negotiations tell BUSINESS

Memos flew back and forth among First International's various intermediaries in 1992, just two weeks before the Democratic convention in July, to pin down final details. One document calls on the buyers to abide by the Saudi boycott of Israel, a violation of U.S. law. Through their attorneys, Brown and Pegado say they are unaware of any such document. Although it's not



FIRST INTERNATIONAL COMMUNICATIONS CORPORATION
2555 M STREET N.W., SUITE 302
WASHINGTON D.C. 20037
Telephone: (202)-828-0814 Fax: (202)-828-4136

MEMORANDUM

TO: Ron Brown
FR: Nolanda Hill
DATE: April 29, 1992
RE: Projects and/or Entities in Which You have a Direct Ownership Interest

ANGOLAN OIL PROJECT:

I have been working with Don St. Clair of FFP Partners, and Gad Zeevi, an Israeli/Kenyan man who... about which, number of... I do not know if you... by DHL the response... I do not have a file in terms of any if so, I did not receive a copy. I do not have a file in terms of any correspondence by and between you and the Angolan contacts and I should have, for continuities sake. If you have not sent the letter we discussed, it is mandatory that you take that action expeditiously at this point as the ball is in your court in so far as I am concerned. I can do nothing else until we have moved in a more formal manner with the Angolan Government.

An Apr. 29, 1992, memo to Ron Brown from Nolanda Hill apprises Brown in detail of the status of a proposed Angolan oil deal. Hill refers to previous correspondence between Brown and "Angolan contacts" and urges him to act quickly.

WEEK.

But that apparently did not dampen Brown's appetite for an oil deal. Through his attorney, Nancy A. Luque, Pegado told BUSINESS WEEK that after he first talked to Brown, he sent a memo to Hill, copied to Brown, about an attractive deal to buy Saudi light crude from Aramco. Pegado, who says through his lawyer that he received no compensation for his role, asserted in the memo that it was possible to negotiate a contract for 50,000 to 100,000 barrels per day. The terms: First International and its consultants would receive a 70¢-per-barrel discount. The final refinery buyer would get a \$1-per-barrel price break to ensure that the deal would be made quickly.

clear why, the Saudi deal also fell apart.

Brown claims the furor over his finances is nothing more than a GOP "smear campaign" to stop him from becoming chairman of Clinton's 1996 reelection campaign, a job change the White House has put on hold because of his difficulties. Representative William F. Clinger Jr. (R-Pa.), chairman of the House panel investigating his finances, has accused Brown of hiding the \$400,000 he received from First International after he became Commerce Secretary. Brown denies the allegation. But that's not likely to tame the increasingly boisterous debate over the silent role that Brown insists he played at First International.

By Douglas Harbrecht in Washington and Paula Dwyer in London

STRATEGIES

FLYING HIGH

Why KLM's global strategy is working



It was a daring move, executed with panache. Even though the Western powers were recognizing Communist China, KLM Royal Dutch Airlines decided in 1983 to become the first European carrier to serve China's arch-enemy, Taiwan. To launch Amsterdam-Taipei service, the airline flew in 10,000 tulips, which Taiwanese authorities auctioned off for charity. The move paid off: For nine years, KLM was the only European carrier to serve Taiwan. It still beats its European rivals for the island's lucrative traffic—and the Taiwanese still remember those tulips.

Imaginative marketing and risk-taking have worked wonders for KLM. Similarly, the Dutch carrier's risky alliance with Northwest Airlines Inc. is emerging as the first successful model of the strategic tie-ups that every airline covets as the industry struggles to globalize. KLM and Northwest are skirting legal and cultural constraints that have stymied other alliances and are pooling resources in the closest thing to a merger their industry has seen.

Their success is not only churning out profits for both partners at a gloomy moment in airline history but is also likely to be a testimonial for deregulation. KLM and Northwest have been able to move their operations mainly because of a Dutch-American "open skies" treaty, which lets airlines of both countries

fly freely into each other's markets. Because they won exemption from U.S. antitrust laws, the two can set prices, market jointly, and may adopt a single name in a few years. Executives of other allied airlines, such as British Airways PLC and USAir Inc., would set off regulatory alarms if they did such things. "We're the only airlines that are building a tight global alliance," boasts KLM Chairman Pieter Bouw.

TAKING NOTICE. As a result of its gutsy moves, KLM has emerged in the big leagues of international aviation. Together, KLM and Northwest are the world's third-largest carrier in revenues, after American and United, a fact that rivals have begun to notice. "They're taking revenues from us," gripes Hans Mirka, vice-president for international services at American Airlines Inc.

Despite such complaints, Washington is convinced more open-skies treaties will ultimately benefit U.S. carriers. So federal regulators plan to use this Dutch-American alliance as a major talking point to pry open other markets. In March, the U.S. will launch negotiations with nine small European countries, from Switzerland to Sweden, to seek similar open-skies agreements.

KLM also is demonstrating how to make money in a deregulated climate. For its fiscal third quarter, the Amsterdam-based airline reported, on Feb. 2, a

NEW DEAL: KLM's costs are among the lowest in Europe

fivefold profit increase to \$49 million. The earnings widely beat analysts' expectations. Overall earnings for the year could quintuple, and sales are expected to rise 11%, to \$5.5 billion. KLM is also enjoying double-digit growth in Asia and Latin America.

KLM's global connections are helping it flourish around its European competitors at home. As Europe's fastest-growing carrier, its market share inside Europe has doubled, to 7%, as it pulls in passengers to connect with North American and Asian flights. Moreover, with \$2 billion in its coffers, KLM will be a key

player in purchasing controlling stakes—or outright ownership—of other European carriers as deregulation winnows out the losers.

KLM's success stands in stark contrast to such rival carriers as Air France, Iberia, Sabena, Alitalia, Olympic, and Aer Lingus, which are kept aloft only by huge state subsidies. Bouw has a bit of advice for his rivals: Accept change as inevitable. Open competition may hurt at first, he admits, but it's necessary to become efficient. If airlines wait, he warns, "they're going to lose out in the global battle that everyone faces."

TAG TEAM

KLM sees its worldwide ties to Northwest as crucial for growth, and the lines are stepping up moves to standardize onboard service

Like many of its
als, the 75-year-old
M used to be a cod-
ed, government-
ned carrier, bred for
colonial empire that's now
inct. The state still owns
% but keeps its hands off.
M's transformation is large-
the work of Bouw, 54. A
-year veteran at the carrier,
he became its boss in
91, then cut costs and
nched a potent growth
ategy. He has added ser-
e around Europe and
aves" of connecting flights
Amsterdam's Schiphol air-
rt, in tandem with North-
est, to create a hub with
st, easy connections to the
S., Asia, and Africa.

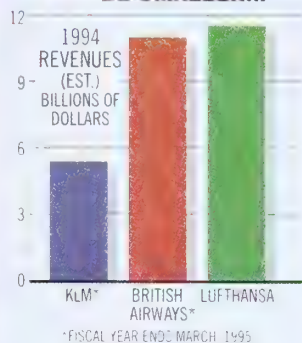
NURTURING. Along the way,
Bouw has rolled up his
sleeves and done plenty of
unt work himself, even
orking out the arcana of
ght traffic. "This is my hob-
," says Bouw—only half-
king—as he bends over a
ack of Schiphol flight sched-
es, searching for more effi-
ent connections.

Yet for all his attention to
tail, Bouw takes pains to explain his
strategy to employees and press them
r suggestions on improving perfor-
ance. By nurturing a partnership with
nployees, Bouw was able to bring
out work-rule changes that have
osted the efficient use of the airline
et. Bouw also has avoided eliminating
single job. Instead, with the same
umber of employees—about 24,000—
e has raised passenger traffic almost
% since 1990. The Dutch carrier's
sts are now among the lowest in Eu-
pe—and continue to drop (charts).

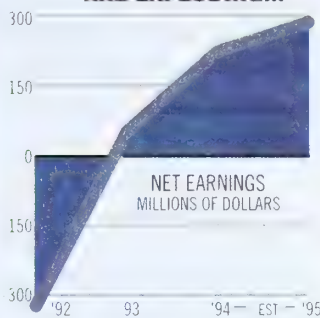
But Bouw's most important move has



KLM: IT MAY BE SMALLER...



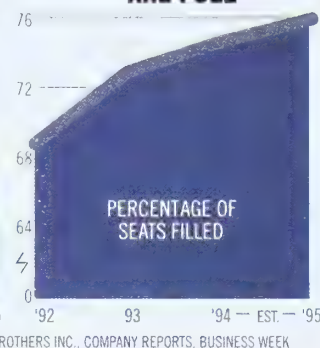
...BUT PROFITS ARE EXPLODING...



...COSTS ARE DROPPING...



...AND PLANES ARE FULL



DATA: NATWEST SECURITIES CORP., SALOMON BROTHERS INC., COMPANY REPORTS, BUSINESS WEEK

been the alliance across the Atlantic. In 1992, three years after buying a 20% stake in Northwest, KLM signed the open-skies accord with the U.S. In return, KLM and Northwest won their unique U.S. dispensation to act as one airline, free of antitrust scrutiny. "We sit down and conspire, we set prices, we share routes—it's wonderful," says Michael E. Levine, executive vice-president for marketing at Northwest.

Their deal lets them cut costs and jump forbidden borders. Rome, for example, is off-limits to Northwest. So KLM, through its European Union privileges, serves Rome on Northwest's behalf—despite Italian government protests. Because of KLM's route system to the Middle East, Africa, and Southeast Asia, Northwest's Levine is selling tickets from Des Moines to Bahrain, "places that weren't on our route map before."

After focusing on their transatlantic connections, KLM and Northwest also want to tighten cooperation in Asia. Northwest is a major presence in North Asia, while KLM has strong route systems in Southeast Asia. And despite the fact that KLM chose Taiwan over China, it can still generate traffic from Beijing and Shanghai via Northwest.

This blossoming of the relationship is proving the wisdom of KLM's risky purchase of its first Northwest stake in 1989. It was terrible timing—the U.S.

airline market tanked in 1990, and Northwest almost went under, thanks to its own overrich leveraged buyout by outside investors. But KLM persevered, although it had to write off its \$400 million investment. Northwest's cost-cutting plus \$50 million in extra operating income from the KLM tie-up have put it in the black. On Jan. 19, Northwest reported a towering \$296 million profit for 1994—topping American Airlines.

Bouw sees only seven or eight global airlines surviving the current consolidation. So KLM and Northwest intend to make the most of their marriage. "They still don't have much product visibility" as a common entity, says Nick Cunningham, analyst at Barclays de Zoete Wedd Ltd. in London. They also need to standardize service, so passengers are willing to fly either carrier interchangeably.

HAPPY MEDIUM. Their cultures also are quite different. KLM gives tiny china houses filled with Dutch gin to business-class passengers. Northwest passes out rock-and-roll CDs. Dutch cabin attendants are formal; Northwest's are too "enthusiastic" for European tastes, says a KLM executive. Bouw hopes to train crews together and mix nationalities for a happy medium.

The partners are trying to blur other differences. Last spring, they launched a common business class, with identical seats, food, and service on international flights. Despite the \$30 million spent advertising the class, some travel agents in Europe say they're not aware of the joint product. This summer, the carriers may introduce a common economy class internationally. It may have video screens in every seatback, with a choice of movies and games. KLM and Northwest would be the first major airlines to offer this perk in economy.

While consolidating the alliance, Bouw has boosted KLM's Northwest stake to the 25% legal maximum. He says he would buy more if U.S. law should loosen, as some in Washington have proposed. Whether or not that happens, KLM is engaged in the industry's first strong effort to prove the merits of global partnering. If the alliance continues to work, it could force the hand of envious competitors around the world.

By Stewart Toy in Amsterdam, with Susan Chandler in Chicago, Robert Neff in Tokyo, and Margaret Dawson in Taipei

**PRITZKER (SITTING)
AND GEOGA ARE
SLICING SERVICES
AND LAYERS OF
MANAGEMENT**



STRATEGIES

WHY HYATT IS TONING DOWN THE GLITZ

The chastened hotelier retools for the cost-conscious '90s

If any hotel group embodied 1980s glitz and hubris, it was Hyatt. From soaring atrium lobbies to a \$700 gourmet picnic it offered atop a Hawaiian waterfall, Hyatt Hotels Corp. oozed excess. Even bloated costs didn't trouble company managers: Anyone who wanted Hyatt cachet, they sniffed, should be willing to pay for it.

But when the go-go market for luxury hotels crashed in 1990, Hyatt got its due. Scores of hotels throughout the industry were saddled with huge debts and unserviceable mortgages. The Hyatt chain, controlled by Chicago's Pritzker family, runs 104 hotels in North America and the Caribbean. The Pritzkers own about one-third of those as well as the land under many other Hyatts. They manage the remainder for other owners—about 30 of whom they had to help restructure after the crash. The

Pritzkers themselves had a stake in one of the biggest flops of the 1980s: a \$360 million resort in Waikoloa, Hawaii. It was unloaded to Hilton Hotels Corp. for \$60 million in 1993.

NEW BOSS. Those experiences have left a much chastened—and far more cost-conscious—company. Although today's Hyatt is hardly a No-Tel Motel, the Pritzkers are retooling the \$2.6 billion chain to banish the image of an all-frills

The wine list has been
decimated, and
Hyatt is even dabbling
in time-shares

hotelier. And as the industry recovers, the Pritzker family, worth an estimate, \$4 billion, is also expanding again. Since early 1994, Hyatt has bought stakes in several new hotels and moved into franchising and time-share resorts. Through a separate family-held chain of 49 hotels and 16 resorts abroad, Hyatt is also developing 30 properties. "There are huge opportunities," says Douglas G. Geoga, 39, who became president last summer after four years as head of development. "We haven't come close to saturating the market."

Geoga, a low-key lawyer, clearly marks the change. While predecessor Darryl Hartley-Leonard was a garrulous marketer who concentrated on building Hyatt's image, Geoga is a dealmaker who wins high marks from Hyatt's hotel owners for his understanding of tightened industry economics. Though Hartley-Leonard remains chairman—and runs a Pritzker-owned events-management company—Geoga appears better positioned to lead Hyatt in an era in which U.S. growth will come primarily through acquisitions.

QUICK FIXES. But first Hyatt had to go on a painful diet. After two decades spent piling on services regardless of cost, Hyatt risked losing many management contracts in the early 1990s. "New owners were becoming reluctant to hire us to manage their hotels," Geoga concedes. So Hyatt looked at what service guests really wanted. Now, they find wine lists pared from 380 bottles to 38. If they want their beds turned down, they must ask. At the Chicago Hyatt Regency alone, cutting the nightly turn-down saves \$220,000 a year.

By eliminating many midlevel jobs, Hyatt has trimmed more than 1,000 from a management staff of 7,100. The chain's once autonomous hotels also now purchase goods centrally. That has cut the number of providers of glass, china, and silver from 24 to 4. And after the chain discovered that it was losing money delivering coffee, it put coffee pots in every room. Altogether, Hyatt has cut \$100 million annually from its costs since 1991. "The trick is not to cheapen our image," says Thomas J. Pritzker, the 44-year-old family scion who is president of Hyatt Corp. "We're cutting where it doesn't hurt the guest." Those gains are lifting the Pritzkers' fortunes—as is a much improved industry outlook: PaineWebber Inc. Managing Director Bjorn Hansson says innkeepers raised room rates in line with inflation last year for the first time since 1987. Hyatt executives say the chain's revenues are up 13%, to \$2.6 billion, since 1990, while gross operating

rs, but the 20-year-old
ests that classic lines
of style.

that Land R

n my book the Range Rover still has no equal when it
comes to the contradictory tasks of providing on-road
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Instead, I casually sipped a cup full
of hot coffee and spilled not a drop.
I was driving a Range Rover.

The Range Rover is a masterpiece with

In 1970, however, Rover did itself
proud with the introduction of what
was at that time the finest 4-wheel-
drive utility vehicle in the world, the
Range Rover. Seventeen years later,
there still is nothing finer. And, at last,
Range Rover is

the massive bearings and other size components

**"IT'S AS IF SOMEONE BUILT A LUXURY
CAR ATOP A LOCOMOTIVE."**

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**We traveled in a
comfort, style, and
confidence only
the Range Rover
provides.**

*No other
SUV has the
Rover's unique
combination
of style,
performance,
and quality*

DESCRPTIONS OF THE ROVER'S
EXTERIOR INCLUDED "the class
classic," "distinctive, impressive and
handsome," "angular but stylish," and "boxy
but elegant." One tester wrote "It's like

The unanimous verdict: If man were
only allowed to own one car, and if that
one car were meant to be the perfect
all-rounder—spacious, comfortable,
powerful, capable of going on where
the roads end—then the choice would
quickly narrow down to one vehicle:
the Range Rover.

**"In short, the
Range Rover is
still the best in
the world at
what it does."**

Really serious car
long acknowledged
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**The Ran
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The Range Rover Classic. We had some help with the name.

For a quarter of a century, Range
Rovers have survived the most brutal
territory in the automotive world.

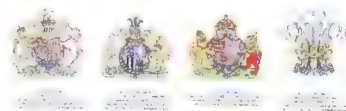
The editorial page.

Therefore, the County Classic needs
little introduction.

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steel chassis, pillowing electronic air
suspension, permanent four-wheel
drive, and tireless 3.9-liter V8 engine
make this Range Rover ideal for driving

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RANGE ROVER

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original Range Rover.

But don't take our word for it.

HYATT'S NEW STRATEGY...

As the hotel industry heats up after four years in the doldrums, here's what Hyatt did to get ready:

CUT COSTS

Centralized purchasing, outsourced housekeeping and valet parking, and cut freebies such as mints on the pillow. Savings: \$100 million annually since 1991.

IMPROVED MARKETING

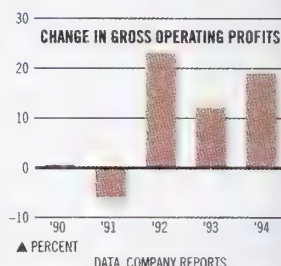
Put fax machines and modems in rooms and beefed up Gold Passport program to attract frequent business travelers.

RENEWED EXPANSION

Spent \$70 million on stakes in four hotels and Atlanta expansion; is eyeing Las Vegas, Philadelphia, and Cleveland and moving into time-sharing and franchising.

DATA: COMPANY REPORTS

...IS PAYING OFF



profits have spurted 45%. And owners' complaints about costs have abated. "Our Hyatt properties have come out [of the depression] quickly," says Allen J. Ostroff, managing director of Prudential Realty Group, which owns hotels in Cambridge, Mass., New Orleans, and San Francisco. "We're very happy."

LOOMING FIGHT. Now, Hyatt wants to grow again. Since early 1994, the Pritzkers have earmarked about \$70 million to buy stakes in four U.S. hotels and refurbish the Atlanta Hyatt Regency. As the improving industry brings hotels on the market—even the entire Hilton Hotel chain may be sold—they've been studying deals. "We looked at Hilton four years ago, and we'll look again," says Pritzker. "Anytime there's an opportunity to increase our scale, we'll pursue it aggressively."

Still, with formidable rivals such as Sheraton, Marriott, and Radisson also in good shape, the industry is heading into a ferocious battle. All are spending lavishly to woo business travelers and resort customers—and focusing limited construction plans on the same secondary markets such as Cleveland and Philadelphia. Adding to the fray, all aim to pluck management contracts away from competitors. Marriott Corp. alone aims to add 100,000 rooms worldwide through acquisitions and new management contracts by 1999—and with its Honored Guest program for frequent-travelers already the acknowledged favorite among wandering businesspeople, Marriott appears little worried about Hyatt. "I'm not aware of any management contracts we've lost to them recently," says Marriott International Senior Vice-President Stephen P. Weisz.

What's more, the search for growth is pushing Hyatt into unfamiliar markets. For the first time, the Pritzkers will franchise the Hyatt name. And with the construction of a Key West resort, Hyatt is entering the crowded time-share market. The moves will bring Hyatt head-to-head with well-entrenched foes such as Marriott and Walt Disney Co.

Rivals are skeptical that Hyatt can shift to such new segments. "You have to have the culture and quality controls to make it work," says Juergen Bartels, president of Carlson Hospitality Group Inc., which owns Radisson. So far, Hyatt has inked just three deals—and Geoga insists it will do nothing to jeopardize Hyatt's name.

Indeed, his challenge now is to ensure that the Hyatt name still has meaning in an industry where brand loyalty is fading. That's why Hyatt is belatedly stoking up its marketing to business travelers. It only recently put muscle

behind its Gold Passport program by offering free air miles. And by blending its fragmented sales force into national teams focused on convention business, Pritzker says, Hyatt has upped group bookings by \$250 million since 1993.

Such improved performance is good news for the Pritzkers and their properties—though not necessarily for rival "I liked it the way they were," says Bartels of Radisson, laughing. "They are going to be a lot more competitive. Although the challenges are steep, few would bet against the revived Pritzkers."

By Richard A. Melcher in Chicago

STRATEGIES

FIGGIE TURNS OVER A NEW LEAF

Under Jack Reilly, the sick conglomerate will be much smaller

No one would ever accuse John P. Reilly, the new CEO of troubled Figgie International Inc., of ducking a challenge. Fresh out of college, he passed up a cushy desk job at Chrysler Corp. to work on the plant floor. In the early 1980s, he helped run a tough downsizing at International Harvester Co. Later, as CEO of Tenneco Automotive, Reilly led a bid by U.S. auto-parts makers to crack the Japanese market.

It all makes good training for the task now facing the 51-year-old Reilly at

Figgie: turning around the ailing Willoughby (Ohio) conglomerate. As recently as 1989, Figgie was a healthy \$1.3 billion company. Starting from a 1963 leveraged buyout of Automatic Sprinkler Corp. of America, founder Harry E. Figgie Jr. built a far-flung empire. More than 30 divisions made everything from fire-fighting gear to sporting goods. But poor management, bad luck, and heavy debt sent the company into a nosedive. A late-1993 cash squeeze nearly drove Figgie bankrupt.

On Feb. 15, just six weeks into his new job, Reilly announced a drastic shrinkage. He aims to pare Figgie to less than a quarter of its former size and use proceeds from asset sales to pay off a crushing \$250 million in bank loans and leases. At the same time, he's hacking away at the bloated overhead left behind by Figgie and his son, Harry E. Figgie III. The moves will leave Figgie with a smaller—but profitable—

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It's how much money
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The Corporation

core, he vows. "It's not how big you are," says Reilly, who has half a million stock options riding on the outcome. "It's how much money you make."

Reilly has announced plans to put at least 15 of Figgie's 22 businesses—including Automatic Sprinkler—on the block. Sales at units Figgie will keep—including Scott Aviation and Interstate Electronics Corp.—total \$319 million. The CEO says all show operating profits.

Reilly estimates Figgie will reap \$300 million from the cast-offs by yearend, which will let it pay down leases and bank loans. That will cut total debt to \$220 million—and with 1995 free cash flow projected at \$41 million, new Chief Financial Officer Steven L. Siemborski says the shrunken company should readily cover its \$25 million in annual interest. Reilly reckons Figgie will return to the black by the third quarter.

To investors who have watched Figgie shares fall from 21 in 1992 to around 7 today, making any money would be a nice change. After losing \$180 million on sales of \$769 million in 1993, Figgie lost \$167 million—including a \$57 million write-off and \$76 million from discontinued operations—on sales of \$762 million in 1994. Wall Street has been wary since Reilly's arrival, but initial reaction to the plan was favorable. "We're generally very pleased with the bold direction that [management has] charted," says Charles K. Gifford, president of the Bank of Boston Corp., Figgie's lead bank.

New direction was certainly needed. When Figgie spurted red ink in 1993, executives blamed a series of one-time problems, such as floods that hit three plants. But an ill-conceived manufacturing revamp, led by son Harry after he in effect took over from his ailing father in 1992, hurt even more. Figgie spent \$200 million to automate but has yet to see the payoff. **"OUT OF CASH."** What it did see was a big jump in debt. Total debt rose \$82 million in 1993, to \$536 million, as Figgie borrowed to pay for equipment. By late 1992, Figgie's banks were unwilling to roll over its loans. It was "out of cash and out of credit," says Siemborski.

To make matters worse, just as the elder Figgie returned to work in late 1993, a former executive filed a lawsuit

alleging the Figgies had diverted company assets to private use and inflated financial results. By early 1994, "the house was burning, and we had to do something," concedes longtime director Walter M. Vannoy, who became chairman in May after Harry Figgie retired. The younger Figgie resigned in March.

The slim-down, announced by the

Reilly says he is keeping only major leaders, such as Interstate Electronics, a \$113 million maker of global positioning systems, and Scott Aviation, a \$1 million maker of emergency breathing systems. With gross margins averaging 22.5%, all have done well despite Figgie's problems—and Reilly is counting on expansion abroad and new products



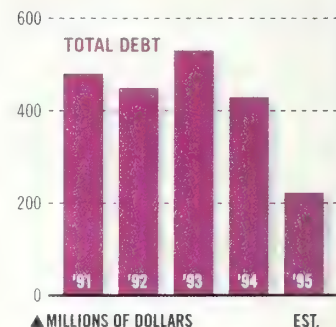
REILLY'S TURNAROUND PLAN...

SELL ASSETS Will unload at least 15 of Figgie's 22 divisions. Annual revenues will shrink from \$762 million in 1994 to around \$359 million in 1995.

SLASH OVERHEAD Corporate art collection and jet have gone. Now, Reilly will ax perks such as a company pool, decentralize, cut corporate staff in half, and slash outside professional fees. Savings: \$22 million annually.

REFOCUS MANAGEMENT Reilly wants an early settlement of a lawsuit charging the board and the Figgie family with mismanagement. Resolving that—and a host of other legal disputes—will slash legal fees and free management to focus on operations.

...SHOULD HELP CUT DEBT



DATA: COMPANY REPORTS

Figgies, got going in earnest after they left. Some \$175 million in assets, including crown jewel Rawlings Sporting Goods Co., have since been sold. And Reilly, who joined Figgie after a brief stint as COO at Brunswick Corp., is slashing overhead—including perks such as a pool. But Figgie still had negative cash flow of \$76 million in 1994.

Will Reilly's plan finally give Figgie the jolt it needs? One question is whether it can get good prices for units it's selling—some of them mediocre performers. But Reilly says he already has letters of intent offering roughly \$100 million for some units. He must also rev up the ongoing businesses.

to double revenues by 2000. "These companies would be very profitable with a normal debt load and normal corporate expenses," he says.

Still, if Reilly has unveiled a new Figgie, problems remain. A settlement of the suit alleging mismanagement is under negotiation, and a host of other legal wrangles are still being fought. But the plainspoken CEO vows these divestiture and write-offs will be the last. "It's absolutely over. This is the end of the line," he says. If Figgie's survival no longer looks in doubt, shareholders may still have to wait for their reward.

By Zachary Schiller
in Willoughby, Ohio

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BLOOD ON THE MARBLE FLOORS

Hundreds of thousands of bank employees could get axed over the next several years

Rampant downsizing has been sweeping across most parts of Corporate America since the early 1990s, producing huge layoffs and shutdowns of operations. Commercial banks, though, have been virtually immune. Despite numerous mergers and consolidations, bank employment has remained remarkably steady. And even though electronic banking is expanding, bank branches, often regarded as relics of the past, have actually increased in number over the past several years.

The comparison between U.S. and international banks is revealing—and chilling, at least for U.S. bankers. As of the end of 1992, Germany had 3.4 bankers per 1,000 citizens. France had 3.5. Japan had 3.7 (as of the end of 1993), and Canada had 4.9. The United States, though, had 5.8 per 1,000. Only Britain, with a unionized banking system, has more bankers relative to its population.

This rather placid situation is unlikely to persist too much longer, however. Major layoffs, involving many hundreds of thousands of tellers, bank office workers, and managers, are likely to take place over the next several years. The reason: Banks, especially those with large retail operations, are increasingly facing stiff competition from brokerage houses, mutual-fund groups, and other financial-services outfits. To fight back, banks will have to shrink severely their single largest noninterest expense: people. Put simply, the nearly 1.5 million people employed by U.S. banks is just far too many.

WRENCHING PAIN. Experts expect the drop in bank payrolls to be dramatic. Seamus P. McMahon, a vice-president at Boaz, Allen & Hamilton Inc., sees employment in branches and traditional offices dropping anywhere from 20% to 50% within the next seven years. "It has to," he says. William M. Riney, senior vice-president for strategic planning at Columbus (Ohio)-based Huntington Bancshares Inc., says there



could easily be 30% fewer bankers in the U.S. by 2000. "There is no way a commercial bank, given its [current] cost structure, can compete with another financial-services provider."

The cuts will cause wrenching pain in an industry that has never gone through such a restructuring. They may also inconvenience a fair number of bank customers, especially those who don't use automated-teller machines or banking by phone. But reducing staff is the only way banks can prevent the price wars that ensue when too many bankers chase too few customers.

The extent to which banks have resisted the cost-cutting logic is startling.

According to the Federal Deposit Insurance Corp., the number of employees of FDIC-insured banks dropped slightly through 1992, but then increased again as lending picked up. As of the third quarter of 1994, employment stood at 1.48 million, almost as high as in 1991.

Much of the staffing bloat can be attributed to regulation. In a number of states, including Colorado and Illinois, banks were long forbidden to have more than one branch. As a result, hundreds of institutions cropped up in relatively small areas, each with its own administration and overhead. Laws limiting interstate banking have produced the same phenomenon. Today, superre-

analysts such as Cleveland's KeyCorp; Charlotte, N.C.'s First Union Corp.; and Providence-based Fleet Financial Group Inc. have numerous different subsidiaries, many with their own treasury operations and boards of directors—not because the banks necessarily want them but because these structures are legal necessities. Altogether, the U.S. has over 10,000 banks, compared with fewer than 60 in Canada, and that means a lot more administrative overhead. It also means worse service in some cases: In Canada, national banks enable customers to deposit checks in Vancouver on one day and withdraw money in Nova Scotia



the next. Some checks take days to clear in the U.S.

Many banks also are still heavily branch-oriented. The number of bank branches in the U.S. stood at nearly 4,000 in June, 1994, up from 47,000 at the end of 1988, according to the FDIC. One reason is that some banks have been buying branches from failed thrifts to expand their customer base. But also, many banks contemplating expense reduction have opted for less controversial and painful cuts.

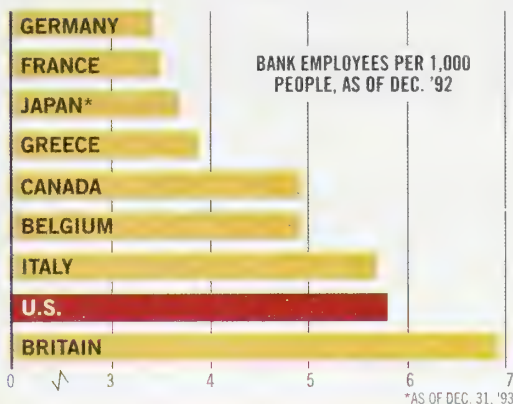
Nonetheless, customers are simply avoiding branches more often these days. The number of ATM transactions has increased 45% since 1990, to 8.3

billion, according to the newsletter *Bank Network News*. And a study by the Bank Administration Institute and First Manhattan Consulting Group Inc. shows that 55% of all retail-banking transactions take place at ATMs or on the telephone.

The escalation of interstate banking will make overstaffing even more apparent. Banks will get a federal green light to expand across state lines without separate charters in 1997, allowing big players to reach into many smaller markets that are already amply served by local banks. The large newcomers will enjoy economies of scale, forcing local banks to slim down in order to

ZAPPED Employment could eventually decline by 30% as a result of stiff competition from nonbank rivals and a fall in demand for traditional services

TOO MANY U.S. BANKERS?



DATA: FEDERAL DEPOSIT INSURANCE CORP., U.S. COMMERCE DEPT., OFFICE OF POPULATION CENSUSES & SURVEYS (U.K.), EUROPEAN UNION BANKING FEDERATION, STATISTICS CANADA, CANADIAN BANKERS ASSN

compete—if they're not swallowed first.

The current economic cycle isn't helping, either. With the Federal Reserve having boosted interest rates seven times since the beginning of 1994, banks are seeing demand for such core products as mortgages simply dry up. That means a lot of bank employees are currently redundant. If revenues remain lackluster—as they probably will while interest rates remain high—banks will have to cut costs in order to generate earnings growth and remain competitive. “Just about anyone running a bank today understands they have to be a low-cost competitor,” says Edward E. Furash, chairman of consulting firm Fu-

rash & Co. “It is one of the rosary beads of current bank management.”

Big staffs are hardly a prerequisite to good service in a bank. Sure, when institutions such as Citicorp have pushed into new foreign markets, they have often forced local banks to upgrade their service in response. But the service in plenty of countries with fewer bank employees per capita is just fine. In Belgium, which has 4.9 bankers for every 1,000 citizens, consumers can pay virtually all their bills by phone in an operation that records both parties' account numbers, the amount of payment, and a notation about what the outlay covers. ATMs are ubiquitous, and debit cards are accepted everywhere from supermarkets to gas stations. Moreover, for the few customers who do use bank branches, the teller lines are short.

PINSTRIPED ROBOTS. Most U.S. banks aren't as technologically advanced, but a few are at least cutting staff. Chase Manhattan Corp., Chemical Banking Corp., and even J.P. Morgan & Co. are shrinking payrolls, partly in response to damage done by high interest rates.

Some banks have also made big strides in automating. Chase even uses robots to help with some of its data storage. In Ohio, Huntington offers its customers a sort of virtual bank containing sophisticated ATMs and interactive-video technology they can use to learn about investments, apply for loans, and even talk to a Huntington banker if they prefer.

Other banks are taking clear steps to rid themselves of branches. PNC Bank Corp. announced in late 1994 that it would consolidate up to 30% of its branches over the next two or three years. Or consider Minneapolis-based First Bank System Inc., which bought Metropolitan Financial Corp. in January, acquiring 211 branches in the process. Instead of holding on to all those branches, First Bank is closing 40 of them and selling 63. When First Bank bought Metropolitan, “what we bought was the customer base—as much as if not more than the branches,” says Richard A. Zona, chief financial officer, and “distribution of various financial products can be accomplished more attractively from a financial point of view through electronics.”

For now, First Bank System's branch sales seem unusually farsighted. But First Bank may not be unusual for long. As pressures on banks intensify, it is becoming increasingly clear that all U.S. banks are going to have to slim down like First Bank—and like the rest of Corporate America.

By Kelley Holland in New York, with bureau reports

SO MANY SECURITIES FIRMS, SO LITTLE SECURITY

It was another dismal week on Wall Street despite improving markets. Salomon Brothers Inc. said it would cut its staff and get out of the retail brokerage business. Goldman, Sachs & Co., which has been laying off scores of investment bankers, reported a capital decline from \$2.26 billion last year to \$1.84 billion this year. CS First Boston announced it would cut or redeploy as many as 1,000 of its 6,500 employees, shutter its municipal-bond department, and exit the Japanese equities business. "Everyone is walking around on eggshells," says one CS First Boston executive.

The main cause of the numerous rounds of bloodletting on Wall Street since last fall is the Great Bond Market Crash of 1994. Its impact has proved far more pernicious than analysts predicted. That Salomon, Goldman, and CS First Boston are hurting most is no surprise: All three firms have large institutional bond operations that got battered when the Federal Reserve began sharply raising interest rates last February. All got caught with large bond inventories that fell in value and suffered big trading losses. Says one Street executive: "Fixed income is like a big flywheel for these firms. When it's hot, it's gigantic. When it's not, they're stuck with the expenses."

"JUST THE BEGINNING." And the pain could continue if interest rates rise again: more layoffs, curtailed expansion plans overseas, jettisoning of more marginal businesses. "If the environment doesn't improve, this will be just the beginning of the Street's restructuring," says Perrin Long, a Brown Brothers Harriman

executive. The underlying problem is the expenses that were built up during years of stellar bond-market profits. Firms became stuck with bloated cost structures that far outstrip revenues, which have fallen

dramatically with the slowdown in underwriting and trading. "The Street has to start looking more closely at its infrastructure costs," says John J. Mack, president of Morgan Stanley & Co.

CS First Boston is a perfect example. The firm plans to reduce expenses by close to 20% to offset a big drop in fixed-income profits. Insiders

have the ballast, such as large money management, custodial services, or correspondent clearing, that helped stabilize some competitors' earnings," says a Salomon spokesman.

Securities firms with strong retail equity businesses, by contrast, are doing well. Charles Schwab & Co.'s stock has risen 25% this year. Earnings for 1994 were up 15%, to \$135.3

million, on the strength of mutual-fund fees, which spiked 59%, to a record \$156.8 million. "The retail firms that haven't been exposed as much to the bond losses last year" are doing a lot better than those that have, says Schwab spokesman Hugo W. Quackenbush.

CONTRARIANS. The stock of Baltimore-based Alex. Brown & Sons Inc., which was up 22% in 1994, has soared another 22% this year, thanks to investment banking and retail commissions. Although St. Louis-based A.G. Edwards Inc. in-

creased its roster of brokers in 1994 from 5,100 to 5,400 brokers, Chairman Benjamin F. Edwards III says: "We've been able to maintain profit margins at 10% or slightly above, and we haven't let anybody go or shrink by attrition."

Several New York houses bucked the bad-news trend as well. Donaldson, Lufkin & Jenrette Inc. had its third-best year in 1994 and has hired real estate bankers from Goldman Sachs and more than 20 emerging-market traders from Bankers Trust. Morgan Stanley says it has avoided layoffs and nabbed mortgage-backed traders from Goldman Sachs. But competitors believe shrinkage at Morgan Stanley is inevitable. Severely reduced bonuses, disclosed to Morgan Stanley employees on Feb. 14, led staff to dub the event "the Valentine's Day Massacre." But, hey, at least they still have jobs.

By Leah Nathans Spiro, with Jeffrey M. Laderman in New York and Russell Mitchell in San Francisco



STREET SIGNS: One exec says workers are "on eggshells"

say that while its muni business generated \$20 million in profits in 1994, the unit isn't profitable enough and isn't a core business. "We don't really expect any significant improvement near-term in market conditions," says Maynard Toll, a CS First Boston spokesman. "It's not prudent to maintain an expense base that was built up during a bull market."

Salomon Brothers left the private-client business for similar reasons: It wasn't an important enough area. But Salomon's main problem is that it is too dependent on bond trading and lacks the diversified revenue stream of a Merrill Lynch & Co. or Morgan Stanley. "Salomon Brothers does not

**One problem:
Expenses built up
during years of stellar
bond-market profits**

UP ON DOWN MARKETS

Brandes Partners discovers diamonds in the rubble



THE BAD NEWS BULLS: Carlson and Brandes are in for the long term when they buy

Bad news has been a good friend to Charles H. Brandes. It was the bear market of 1973 and '74 that nudged Brandes to quit his job as a stockbroker and open his own global money-management firm. Now, 21 years later, Brandes Investment Partners manages a tidy \$4 billion from its home base near the crashing Pacific surf in Del Mar, Calif. But its 51-year-old under, a dedicated value investor with a eye for cheap stocks, is still a bad news bull.

Currently, Brandes and his dozen young analysts are sifting through the rubble of emerging markets from Latin America to Asia looking for nuggets others have discarded in their scramble to avoid the aftershocks of Mexico's peso collapse. Says Brandes: "The markets are very inefficient and manic-depressive. And wrong a lot."

Betting that the markets are wrong as paid off for Brandes and his investors, a well-heeled lot who must ante up at least \$100,000 to get in the money manager's door. Over the past 10 years, Brandes' international equity portfolio has returned a tidy annual return of 23%—nearly five percentage points better than the widely watched Morgan Stanley index of European and Asian stocks. **BUNKED.** Amid such high returns, Brandes' assets have mushroomed 1,500% in just six years. Last year, however, proved that even home-run kings sometimes strike out. Rising interest rates and political turmoil hit such Brandes favorites

as Hong Kong, Spain, and Italy, leaving investors nursing a 3% loss for 1994 after a 41% gain in '93. But Brandes says one year's losses shouldn't make or break an investment strategy. He prefers to hold stocks for at least three to five years and cautions against buying whatever is faddish. "What's a good stock for 1995?" he asks. "That's not the right question."

Nevertheless, several gems have popped up on the firm's screen for long-term value (table). Brandes' right-hand man, Glenn R. Carlson, is prospecting in Argentina, where stocks have been brutalized by fears of currency devaluation. Carlson's top pick: YPF, a big oil producer that trades at only 3.7 times cash flow. Brandes is less sanguine about Mexico. Still, he continues to like Teléfonos de Mexico, the peso-shocked phone giant, whose American depository receipts have plunged since 1994. That has left Telmex' price-to-cash flow ratio at a mere 5, well below the 5.7 average for the slower-growing Baby Bells.

Brandes also is eyeing several value plays among smaller U.S. regional thrifts. His top pick: IBS Financial, based in Cherry Hill, N.J. It has lots of cash left over from an IPO and could be a takeover candidate in the current wave of industry consolidation.

Although he's a long-term investor, Brandes is not afraid to sell out—even if it's unfashionable to do so. In 1990, Brandes bought Compania de Teléfonos de Chile, then a newly privatized utility, for \$12 to \$15 a share. The stock, he recalls, "was being ignored in spite of the fact that Chile was one of the most successful economies." Less than a year later, with Latin stocks sizzling, Brandes sold CTC for \$37. He now makes a similar case for

another out-of-favor stock: France's Alcatel Alsthom. A giant power-plant builder, cable manufacturer, and the maker of the French TGV bullet train, Alcatel has seen its stock decimated by managerial and financial embarrassments. Now trading at \$18, its ADRs were \$29 only a year ago. But Brandes notes the company still has a strong balance sheet and rich free-cash flow. And it's trading at a third of the cash-flow multiples that global competitors are fetching.

SMALL-CAP PLAY. To identify the Alcatels of the world, Brandes looks for low ratios of price to cash flow, book value, and earnings, among other things. His analysts examine corporate accounting standards and business prospects, then hit the road to visit companies. But even if all screens flash "buy," Brandes strictly limits how much money can go into any one company, industry, or country. The firm never has more than 20% in emerging-market stocks, and it limits the number of equities in each portfolio

to 30 or 40. "We want our stock ideas to have an impact," says Carlson.

Despite last year's weak results, Brandes recently began offering a portfolio of small-capitalization overseas stocks. Next month, he'll launch his first mutual fund, which will invest only in non-U.S. stocks. Around the world, Brandes says, "equities are where the wealth is produced." And from a value standpoint, the more bad news the better.

*By Nanette Byrnes
in Del Mar, Calif.*

Brandes' Favorite Value Plays

		PRICE PER SHARE
TELEFONOS DE MEXICO MEXICO	Rocked by peso collapse but offers cheap cash flow	\$30*
HSBC HOLDINGS BRITAIN	Deep-pocketed owner of Hongkong & Shanghai Bank has strong China ties	\$10
YPF ARGENTINA	This oil producer trades for less than four times cash flow	\$20*
FUJI PHOTO JAPAN	Plenty of cash—and the stock is down 8% since January	\$44*
IBS FINANCIAL U.S.	Another cash-rich bank. And it may become takeover bait	\$11

*Price per American depositary receipt

DATA: BRANDES INVESTMENT PARTNERS

ILLUSTRATION BY JIMMY K. HARRIS



NOBODY KNOWS HOW HIGH THE QUAKE REPAIR BILL WILL BE

STOCK MARKETS

JAPAN'S MARKETS HAVEN'T STOPPED SHAKING

And the consensus is that the Nikkei will fall further

Aftershocks from the earthquake that hit Japan on Jan. 17 are still rumbling through Tokyo's stock market. Uncertainty about the size of the repair bill, how it will be paid, and what companies will benefit has confused investors and sent the Nikkei stock index on a wild roller-coaster ride. After plunging to 17,785, the index climbed, then dipped, and by mid-February was hovering at 17,991 (chart).

Don't expect much improvement. Indeed, a consensus is forming that the Tokyo market is heading downward—at least over the short term. The aftermath of the quake could force interest rates up and divert powerful savings pools controlled by the Japanese government away from the market and into the reconstruction effort. On top of that, no one seems to know what the true earnings picture is for many Japanese companies; since the earthquake has disrupted sales for some while fattening order books for others. Says Jason James, strategist at James Capel Pacific Ltd. in Tokyo: "The quake was a clear negative for the market."

To be sure, almost no one foresees a major crash. That's because the Japanese government would likely intervene

with the "price-keeping operation" it has used in the past when shares sink so low that banks' equity portfolios can no longer cover bad-loan write-offs. A PKO means injecting public funds into the market and jawboning private institutions into helping out.

But because of the quake, the government may have less money at its disposal to buy shares this year. In recent years, the government has customarily orchestrated an upturn in the Nikkei in February and March, after companies and banks sell off shares to bolster their balance sheets before the fiscal year ends. Now, some analysts fear that rebound may not happen—or prove much weaker—because of strained government finances. In addition, Alexander Kimmont, vice-president of Morgan Stanley Japan Ltd., worries that the government may channel money from the postal savings and life insurance systems, which it normally uses for PKOs, into loans for rebuilding.

The short-term economic pressures on the market are formidable. For starters, reduced consumer spending may slow Japan's recovery as frightened Japanese squirrel away more money for the next big temblor. Department stores and other retailers report a recent drop-off in traffic.

More important, perhaps, interest rates seem poised to move higher; the government starts issuing possibly \$70 billion or more worth of new bonds to pay for quake rehabilitation. Analysts see yields on benchmark 10-year government bonds going to 5.4% from current 4.6%. Money invested in the more attractive bonds could divert funds from the stock market.

Individuals and companies needing to rebuild assets lost in the quake may have to sell shares to raise cash. That could help send the market down to 17,000 or as low as 16,000, says James Capel's James. That's when the government would probably initiate a PKO.

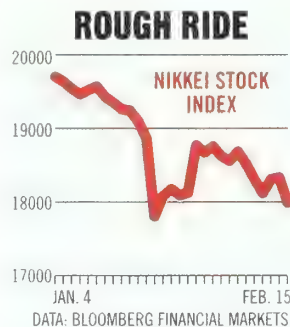
BIG GAINS? As the cleanup continues, investors' eyes will turn to earnings. James Capel believes quake-related expenses will pare corporate earnings growth to 8% from a previously forecast 20% for the fiscal year ending in March, although the firm projects 35% earnings growth for the next fiscal year. Still, the Nikkei is selling at a mind-numbing price-earnings ratio of 74.

But the true earnings picture could be clouded if companies use the quake as a pretext to charge off other items. That could further confuse investors. The market has already discounted quake-related gains for construction companies, whose share prices rose just after the temblor, then dipped sharply. Shares of electronics companies and department stores have also dropped.

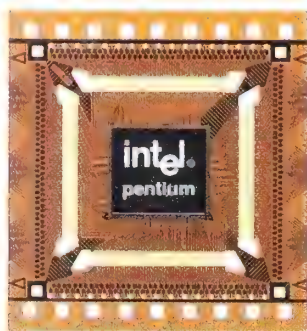
Despite all the short-term bears in Tokyo, there are enough bulls who say it doesn't pay to worry too much about Japan's market for the long haul. Even with new pressure on interest rates and government savings pools, the Nikkei could return to 22,000 by year-end, they argue.

John F. Bahrenburg, senior strategist at Merrill Lynch Japan Inc., predicts equity prices will surge 40% to 50% over the next five years. Perhaps. In the meantime, and especially this spring, investors should be braced for rougher times.

By Robert Neff in Tokyo



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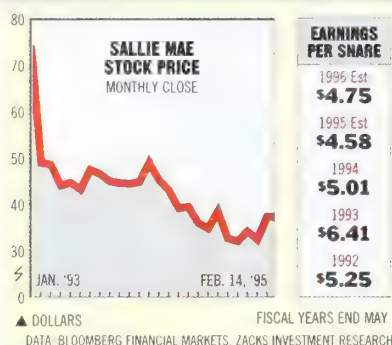
BY SUZANNE WOOLLEY

WHY SALLIE MAE MAY SALLY FORTH

Value investor Harvey Eisen, who advised keeping cool and searching for bargains in the 1987 crash, is still finding undervalued issues in a market that has doubled since then. The senior vice-president for equity investments at Travelers Group offers up two nifty picks.

Eisen calls his first stock, Sallie Mae—the Student Loan Marketing Assn.

WILL SALLIE ACE THE FINAL?



(SLM)—a “Newt play.” Sallie Mae has taken a beating since the government announced in 1993 that it would begin making federally insured student loans directly. By 1998, the government wants direct loans to account for 100% of such loan volume. The stock fell from 75 to a low of 32 and now trades at about half its 1993 high. But with all the Newtspeak about downsizing government, Eisen says the outlook for Sallie may be rosy again. “It’s a terrific risk-reward story,” says Eisen. “It’s a big-cap name, the stock is down, and it’s a high-quality business.”

If the government backs off from making direct loans, it could mean rising earnings—and a rising stock price for Sallie Mae. Using a figure of 10 times earnings, vs. its current anemic price-earnings ratio of 8, Eisen reckons the stock could hit 50 in 1995.

Eisen’s second pick: an up-and-comer called WorldCorp (woa). It is in two very different businesses—one a potential gold mine, the other a mundane money-loser.

One unit, U.S. Order, develops hardware and software for such electronic transactions as home banking, home shopping, and other interactive service.

es. Visa International paid \$15 million last August for exclusive rights to its home-banking technology and pays U.S. Order a royalty of \$8 per year for every customer signed up for the next seven years. Visa has 390 million cardholders worldwide. If it gets just 2.5 million subscribers, that means roughly \$20 million a year—for a company with overhead of \$6 million. So far, close to 40 banks have signed on.

Eisen sees huge potential. “Visa, a worldwide organization, is saying, ‘This company has what we want.’ It’s a major step toward home banking and the elimination of paper checks,” he says.

The mundane part of WorldCorp: international air cargo. Its carrier operates at a loss, but 24.9% of it has been sold to a Malaysian outfit for \$27 million, putting the value of the business close to the company’s market capitalization.

Trading at 8½, WorldCorp gives investors World Airways and, in effect, a warrant on U.S. Order’s technology, says Stephen D. Weinress of L. H. Friend, Weinress & Frankson. Another kicker: A spin-off may be in the works. U.S. Order President John Backus says that several investment banks and WorldCorp investors have approached it about doing an initial public offering and that WorldCorp is “actively considering” an IPO of 20% of its 91% stake in U.S. Order. “This is as open-ended a story as I’ve ever seen,” says Eisen.

A CABLE OPERATOR WORKS THE PHONES

For another undervalued stock with a Newt connection, try Jones Intercable (JOINA). The innovative cable company, which carries Gingrich’s class, “Renewing American Civilization,” on its continuing-education channel, trades at around 15. But it could be worth almost twice that, according to money manager Scott M. Black, president of Boston’s Delphi Management.

Fear of rate rollbacks and competition from telephone companies has cable stocks out of favor. But Jones

Intercable has a link with a phone company: Bell Canada International, which has bought 30% of Jones. Since Bell Canada and Northern Telecom are both owned by Canadian company BCE, Jones has good access to technological developments. It also has entrée in Britain through its stake in Bell Cable Media (BCMPY), a British outfit formed last year by Bell Canada, Cable Wireless, and Jones.

Even in a tough environment, Jones is growing. Cash flow increased 6% in 1994. When Black tallies up the company’s \$60 million in cash flow, value of the cable-TV station at \$660 million, throws in Jones’s stake in Bell Cable Media and a potpourri of other businesses, and subtracts debt, he arrives at a breakup value of about \$25 a share. That’s \$2.50 less than what Bell Canada paid the company for 7.5 million shares last December. Black has 100,000 shares and is still buying.

THE UPSIDE OF UPJOHN

Merger rumors have long swirled around Upjohn (UPJ). But Oppenheimer investment strategist E. Michael Metz, who thought Upjohn would be taken over last year, says the drug giant may make it to the altar in 1995. What’s different now?

Freedox fears, says Metz. The drug, which aims to prevent secondary tissue damage from neurological injuries, is one of Upjohn’s major new-product efforts. Clinical trials are ongoing, but enrollment in the U.S. was suspended after a safety commission saw a higher mortality rate in patients on the drug than on a placebo. “Upjohn put a lot of confidence in Freedox,” says Metz. “Now, it’s highly questionable whether it will succeed. Upjohn can’t tell shareholders to wait six months for a blockbuster product.” An Upjohn spokesman says: “We continue to believe in Freedox.” Is merger pressure on? Upjohn declined to comment.

A domestic buyer who could cut duplication in marketing and R&D to plump up the bottom line might pay as much as 50, says Metz. A foreign buyer might pay handsomely to get Upjohn’s R&D skill. The stock trades at 34. Investors get a 4.4% yield, and the dividend looks safe, since Upjohn has little leverage and no external capital requirements. The stock sells at a below-average p-e of 12.

WIRED FOR THE FUTURE



WHAT'S MIRIAM BERGMANN'S SECRET TO CULTIVATING AWARD-WINNING RIGOLETTO DAHLIAS?



(IT AIN'T THE WATER.)

Silicon Valley Arts Fund is a 501(c)(3) non-profit organization. Photo by Peter Dinklage.

*S*ure, they need the moisture, but the little darlings really perk up to the classics," said Miriam.

It occurred to her at the San Jose Center for Performing

Arts. She made the intuitive leap during a particularly stirring passage of Stravinski's Rites of Spring. Miriam, and her dahlias, can be a lesson to us all: a community endowed with a healthy portion of the Arts enriches the lives of all who live there.

But the numerous, quality Arts groups within the Valley can't continue to enrich our lives if the groups themselves are undernourished. The Arts need money to grow.

Enter the Silicon Valley Arts Fund. This unprecedented project creates the financial foundation on which the Valley's Arts



groups can prosper and grow. Without it, the Arts, like any entrepreneurial Silicon Valley business, would be locked into a start-up mode.

We are calling on those in positions to support a thriving community of world-class Arts to do so. And make no mistake, we're seeking major investors. Because an investment in the Arts Fund is nothing less than an investment back into the fabric of Silicon Valley. It's present. And it's future. So that for many seasons to come, music, dance, theater, the visual arts, and imaginations, can spring eternal. After all, this used to be called the Garden Valley. To talk seriously about supporting the Silicon Valley Arts Fund,

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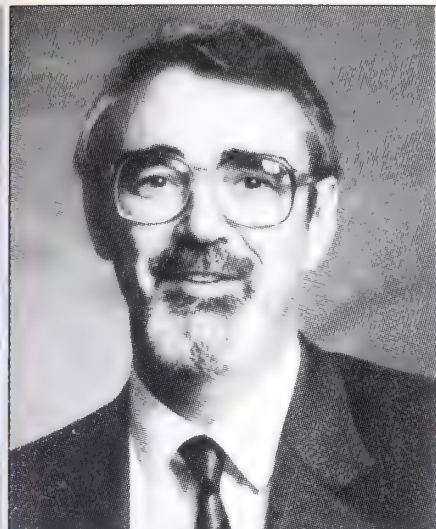
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21ST-CENTURY CAPITALISM

AND ITS IMPACT ON AMERICAN BUSINESS



AL MOSCHNER
President and Chief Executive Officer
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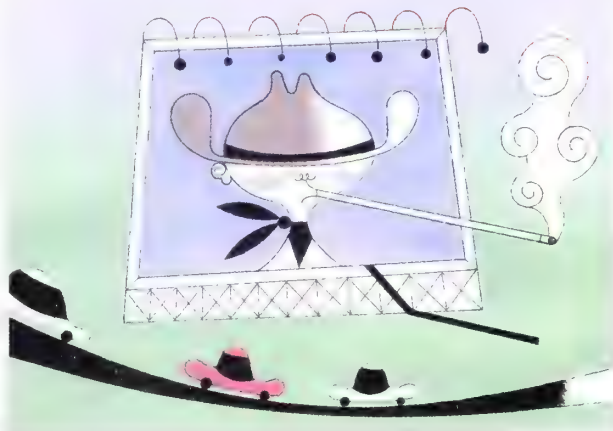
NEW UNIT OF BRITAIN'S General Electric Co. PLC is developing an ink concentrate that delivers sharper pigments at a lower price per page. MICAP Technology Corp. in Niles, Ill., a year-spin-off of GEC's A.B. Co., uses fine grains of pigment less than 10% the diameter of standard particles. Then it coats the pigment grains with a polymer. The substance, in the position of which MICAP won't reveal while patent applications are pending, leads to the chemically ac-



MICAP INK CAPSULE

sites on the particles so they don't cling to one another, a common problem in ink that results in uneven coverage.

MICAP Ink Capsules cost less per pound than standard films. But because they spread more evenly, less ink is needed to coat a page, lowering the net cost, says Robert A. Lustenader, MICAP's director of operations. Another advantage: The ink is less polluting because no solvents are required to mix the capsules with the ink's varnish. And because the ink layers are thinner, they dry better. MICAP is prepared for volume production of the first formulation, which is for sheet presses, and Lustenader says the company is testing formulations for web presses, including those for newspapers.



HOLOGRAMS THE SIZE OF BILLBOARDS?

PICTURE A 100-TIERED WEDDING CAKE WITH THE SIDES of each layer sloping slightly inward toward the bottom. If the cake is made of glass and the sides are coated with silver, you've got a stack of lenses that can be used to create holograms or focus X-ray lasers for production of superdense computer chips. That, anyway, is the concept behind a U.S. patent awarded late last year to Carl R. Amos, an independent inventor in Reston, Va.

Amos says holograms made with his device would be viewable from any angle, making them suitable for, among other things, billboards. He says that's because in forming the hologram, part of a laser beam coming through the bottom of the "wedding cake" fans out over a wide area. Walter M. Gibson, director of the Center for X-Ray Optics at the State University of New York at Albany, says Amos' system seems to be unique—but he can't vouch for how well it would work.

THESE MARKERS MAY GIVE CANCER TESTS BETTER MARKS

BLOOD TESTS FOR CANCERS of the colon, prostate, and ovaries are often inaccurate. One problem: Normal, non-cancer cells may also bear the protein markers picked up by the tests. Searching for better markers, scientists at Matritech Inc. in Cambridge, Mass., and at Johns Hopkins University have identified a dozen so-called nuclear matrix proteins (NMPs). Each one is specific to a single type of cancer and is not found in

any other cell. The first NMP test, for bladder cancer, goes on sale in Europe next month.

Detection is just the beginning, says Matritech Chairman and Chief Executive Stephen D. Chubb. If the proteins regulate tumor growth, drugs should be able to block their function and slow the cancer. Unlike existing cancer drugs that attack all rapidly dividing cells, NMP therapies should leave healthy cells untouched. Now, backed by a grant from the National Cancer Institute, Matritech hopes to clone the gene that expresses an NMP specific to prostate cancer.

INNOVATIONS

■ AUSTRALIAN RESEARCHERS at the CSIRO Division of Materials Science & Technology in Clayton, Victoria, have found a way to generate X-ray images while sparing patients high doses of X-ray radiation. The trick: The scientists measure diffraction to detect how various tissues slow the X-rays differently, in addition to the traditional approach of measuring differences in absorption by tissues.

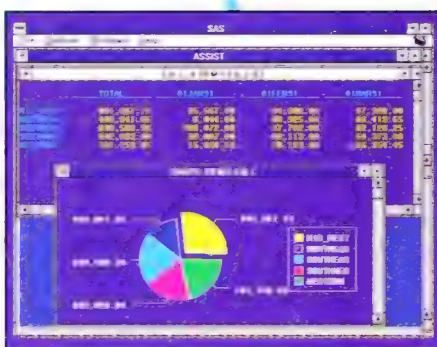
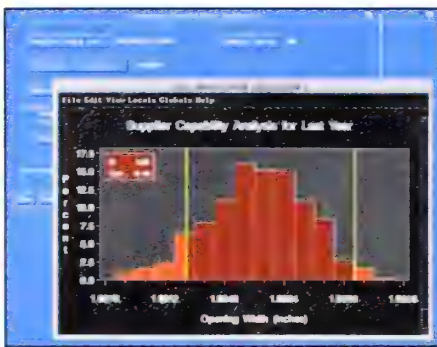
■ THE ARGONNE NATIONAL Laboratory says a bathtub-size "electrorefiner" could process a ton of spent nuclear fuel a day. The device uses electric current to separate plutonium from shorter-lived wastes such as cesium and strontium. To make it operate quickly, Argonne reduced electrical resistance by putting electrodes close together and increasing their surface area.

■ MULTICHIP MODULES MAKE computers faster and smaller by cramming several chips into one package. Trouble is, they're expensive. Dow Chemical says its new chemical, called Cyclotene, should make multichip modules cheaper to manufacture. Cyclotene can be coated into multiple layers of extremely thin films on which copper circuits can be laid out. Unlike polyimide, its nearest competitor, it doesn't corrode copper circuits or absorb water. And it goes on flat and smooth with one coat.

■ AT SIEMENS CORPORATE Research in Princeton, N.J., they've developed a graphic language called Gestalt that makes it easier to spot bugs in big software projects. Gestalt helps designers create a master plan for their program. Then it checks whether connections between pieces of code are "permitted" by the architecture—and highlights them in red if they're *verboten*.

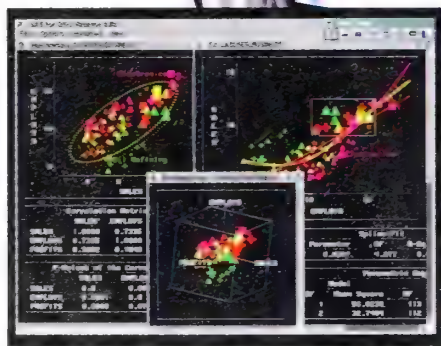
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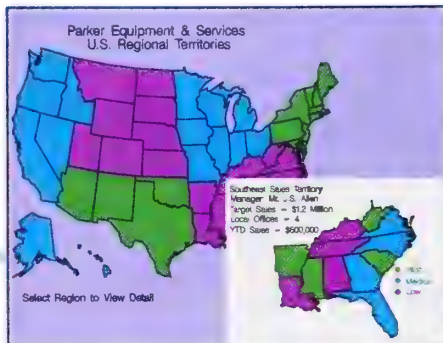
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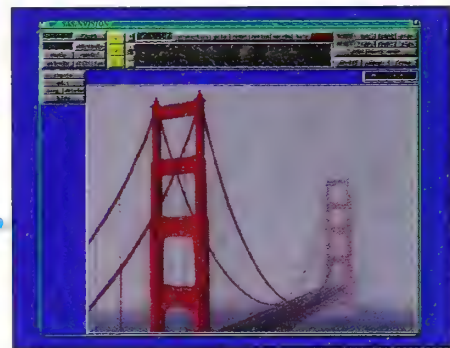
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'GADFLY BOB' IS IN THE CATBIRD SEAT

The controversial plans of House Science chief Bob Walker

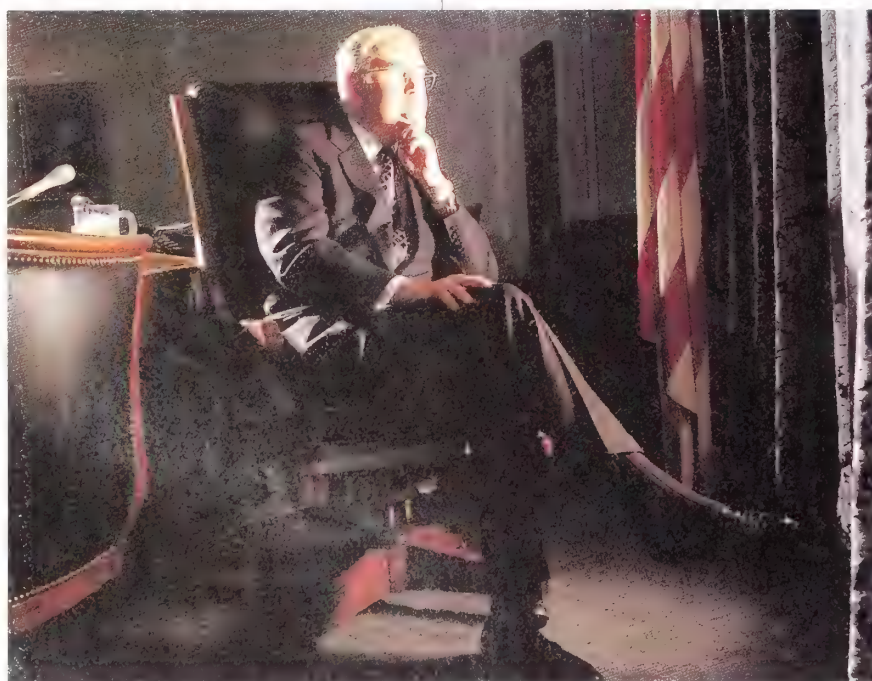
Ever since Pennsylvania voters sent him to Congress in 1977, Representative Robert S. Walker has been one of the Republicans' most aggressive zealots. He led fierce, losing battles against Clinton Administration programs he considered ill-conceived "industrial policy" or plain dumb, especially plans to boost funding for research and development in industry. Walker even brought a staffer's pooch to Capitol

His committee has rushed to pass legislation requiring risk assessments and cost-benefit analyses before agencies issue major rules, with the goal of easing the regulatory burden on companies. He's also sponsoring a bill to redirect \$100 million of Energy Dept. money to hydrogen research, a fuel he believes "has amazing potential." And he's about to reassess how the government stimulates science and technology, which could

That's a welcome message to the science community, which expects him to shield funding for basic research.

But many research mavens worry that Walker's enthusiasm is marred by misunderstandings and contradictions. He insists that the "federal government's role should be limited to large basic research." However, industry experts say drawing stark lines between applied and basic research is impossible. "Walker is naive about how R&D operates in a corporation," says one chemical-industry executive. Indeed, "many of his ideas may turn out to be totally off-the-wall," adds Representative George E. Brown Jr. (D-Calif.).

WHIPPING BOYS. Walker's preferred whipping boys are Clinton programs such as the \$431 million Advanced Technology Program (ATP) at Commerce and the \$443 million Defense Dept. Technology Reinvestment Project (TRP), which fund high-risk research of interest to companies. He calls the programs a



WALKER: Is his enthusiasm for science marred by a naiveté about research?

Hill to sniff a solar doghouse developed by the Energy Dept. "Gadfly Bob," Democrats called him.

Today, the 52-year-old Walker no longer has to fight what he calls "a guerrilla war." With the GOP victory in November, "we gadflies are now the system," he says. As chairman of the

Science Committee, vice-chairman of the House Budget Committee, and a close friend of Speaker Newt Gingrich, much of the Walker's agenda may hinge on policy.

lead to more general tax credits and funding cuts for specific technologies. "He's not just 'Crazy Bob,'" says a veteran Democratic aide. "There's a lot of substance there, too."

As Walker, a licensed race-car driver and Corvette buff, roars into the fast lane, some technology experts question if it's the right substance. Walker holds a passionate belief in the power of science and technology to transform and improve society. "We can invent our way out of many problems," he says.

THE WALKER AGENDA

The Republican victory has transformed Representative Robert S. Walker (R-Pa.) from "gadfly Bob" to Congress' statesman of science. Here's what he wants to do:

- Focus government spending on basic research, ending federal efforts to develop specific commercially important technologies
- Stimulate industrial R&D through tax policies
- Base regulations on more rigorous risk assessments and cost-benefit analyses, preventing agencies from issuing onerous rules
- Redirect energy research to encourage hydrogen technology
- Encourage companies to explore more commercial uses of space
- Explore whether research on global warming may be biased toward proving that warming is occurring

step toward a misguided industrial policy. The nature of government "makes it impossible to pick winners instead of losers," he says. In fact, Republicans are trying to rescind money already appropriated for these programs.

That's a big mistake, says J. Michael Bowman, vice-president for advanced materials at DuPont Co. Federal funds, he says, support fundamental science, not product development, as Walker's staffers claim. "The Republicans don't have a good understanding of the pro-

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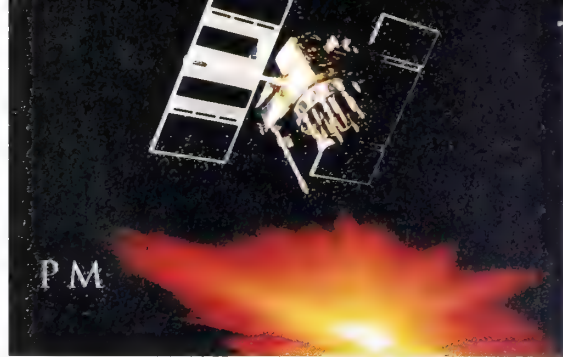
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grams," Bowman says. Victoria F. Haynes, vice-president for research at B.F. Goodrich Co., adds that federal funding also helps now that global competition has caused companies to cut back long-term research. "It's accepted that government R&D helps make our country strong," says Haynes. "But let's spend the money on programs that have more direct benefit to industry."

Walker's critics also point to exceptions to his opposition to government funding for commercial technologies. He is a big fan of Pennsylvania's \$25 million Ben Franklin program, a state-corporate partnership that funds technology research, which K. Jack Yost, who oversees a Franklin center calls "an amalgam of TRP and ATP." Walker's response? With state-run efforts, he says, "you wouldn't get the industrial policy" since the programs respond to local needs.

FUEL FRACAS. In addition, opponents charge, Walker has no compunction about throwing taxpayers' money at areas of research he favors, such as hydrogen. Walker's bill would pump millions into research and development for everything from new ways of making hydrogen to hydrogen-powered cars and planes. "He is moving ahead full steam with industry," observes Brown. "It is a contradiction, but don't point that out."

Not at all, retorts Walker. "Hydrogen isn't a technology, it's a vast field of study," he says. And as a clean fuel, it "has the potential to reduce the regulatory burden." Still, even some Republicans recognize that there's no quick, easy path to a hydrogen economy. "Hydrogen has a lot of problems," says Representative Vernon J. Ehlers (R-Mich.), vice-chairman of the science committee.

The bigger issue, however, is the overall policy direction. Under Clinton, the government has doled out money to companies to help develop tomorrow's technologies. Walker is sure there's a better way. "Small entrepreneurial firms on the leading edge feel that changes in capital-gains treatment are vastly more important than any government programs," he says.

Walker is also exploring the idea of killing programs such as ATP and using that money to give companies an expanded R&D tax credit. It would cover their own research and also facilities and research they fund at universities. But with the GOP so concerned with balancing the budget, Congress isn't likely to adopt his approach anytime soon.

Yet Walker is unfazed. "There's a calmness that comes from knowing you have the votes," he says. With his new position and the GOP majority in Congress—he will have a profound impact on Washington's science and technology policy.

John H. Johnson, Washington

Sports Business

EARLY POINTS: JOHN HANCOCK SPONSORS
PRE-OLYMPIC BOXING TRIALS



ATLANTA OLYMPICS

LET THE HYPE BEGIN

The name of the 1996 games: Move fast, watch your back

On Mar. 7, Atlanta Olympics czar William P. Payne will auction off a one-of-a-kind Hanes T-shirt emblazoned with the logo of the 1996 games and the number 500 as the countdown to the opening ceremonies begins. At Home Depots nationwide, people are shelling out \$35 for personalized bricks that will go into the building of downtown Atlanta's Olympic Park. Ticket-application forms will be available soon at Home Depot and Coke displays everywhere. And NationsBank is underwriting the rehabbing of rundown housing near the Olympic Stadium.

With just 17 months to go before the 1996 summer games, Olympic sponsors are kicking into high gear (table, page 118). After paying as much as \$40 million apiece to link their identities with the five linked rings, companies are whipping up costly programs to help them cut business deals, launch new products, motivate employees, and wrap their advertising in the glory of the gold. Meanwhile, wary Olympics officials are laying plans to protect sponsors from "ambush" advertising that could steal the thunder from their sanctioned efforts. And the Atlanta Committee for the Olympic Games (ACOG) is scrambling to sign 20 more sponsors—and keep its original budget plan on track.

Indeed, ACOG must move swiftly. A

zealous Payne & Co. promised Atlanta an Olympics that wouldn't cost taxpayers a nickel. The original plan called for ACOG to net \$650 million in sponsorships and licensing fees, fully 40% of the games' projected total revenues of \$1.6 billion. But many would-be global sponsors balked at the original \$40 million asking price for 10 major categories. Payne had to backtrack, parceling out smaller bits of turf. He now expects to sell sponsorships in as many as 50 different categories to net the \$650 million. **NO PIGGYBACKING.** Even so, many categories are going begging. No domestic auto company has signed on despite Payne's assertion in mid-February that a deal is imminent. To help move the sponsor hunt along, ACOG now is using an anti-ambush program as part of its sales pitch. The message: If you pay to sport the Olympic rings, rivals won't be able to horn in. ACOG officials bristle at the very mention of ads aired during last year's Lillehammer Winter Olympics by Wendy's International Inc., a non-sponsor that featured founder R. David Thomas in Olympic settings in its advertising, causing more than burgers to fly at official sponsor McDonald's Corp. Last summer's World Cup was a veritable free-fire zone for ambushers, with non-sponsor PepsiCo Inc. using soccer legend Pelé to push Pizza Hut World

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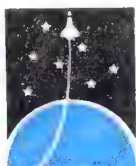
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Fidelity Investment Challenge



LEADERS

Update #5 • Closing Values as of 2/1/95

Here are this week's leaders in the Fidelity Investment Challenge. On November 4 over 3,500 amateur investors began trading with a fictional \$250,000 portfolio. Over the course of the next 3 months, they will buy, sell, or short sell any stock listed on the NYSE, AMEX, or OTC.

At the conclusion of the competition, February 10, 1995, the participant with the highest equity value will win a Eagle Vision TS1 plus 2,000 in cash. Other participants will win cash. Fidelity OnLine Xpress™ software and Market Master t-shirts for their performance.

THE TOP 30 AMATEUR INVESTORS

Rank	Investor	City, State	Equity Value
1	Jay Plisco	Cold Spring Harbor, NY	\$579,850
2	David Evansen	Boca Raton, FL	\$439,099
3	Richard Barron	Rockville, MD	\$418,711
4	Jim Jacobsen	Somerset, KY	\$406,804
5	Gart Bermas	Frammingham, MA	\$398,798
6	Gregory Spencer	Sarasota, FL	\$391,131
7	Yitzhak Peykar	Brooklyn, NY	\$382,409
8	Raymond A. Olsen Jr.	Ocean Grove, NJ	\$379,090
9	Robin Ashworth	Covington, KY	\$378,604
10	George Mergenonov	Longwood, FL	\$373,550
11	Mike Gilledder	Morristown, NJ	\$372,196
12	Anatoly Raklyar	Brooklyn, NY	\$368,603
13	Steven Butler	Ronkonkoma, NY	\$357,614
14	David Swanson	Glenview, IL	\$355,083
15	William Miller	Murreesboro, TN	\$353,112
16	Phillip Zogran	Stuart, FL	\$353,107
17	Fenton Scruggs	Cleveland, TN	\$349,950
18	Pete Elliott	Austin, TX	\$349,510
19	Eric Baird	New York, NY	\$345,754
20	Rupert Boeselt	Lott, TX	\$344,155
21	Jamie Weiss	Portsmouth, NH	\$340,093
22	Brian McKay	New York, NY	\$337,962
23	Ted Campbell	Deerfield, IL	\$337,337
24	Shirley Lyter	Seattle, WA	\$337,287
25	Henry Sodke	Austin, TX	\$335,125
26	Pr M.K. Adil	Cumberland, RI	\$332,672
27	Charles Lechialo	West Newton, MA	\$332,007
28	Mike Becich	Wexford, PA	\$330,843
29	Stanley Moore	Corvallis, OR	\$330,039
30	Robert Sonius	Nicholson, PA	\$329,605

THE COMPETITION UP CLOSE

Average Portfolio Value	\$240,049
Average Percentage Increase	-3.98%
Average Number of Trades Used.....	41
Portfolio Value of the 100th Ranked Account.....	\$295,985

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REPLICA

wide outside the U.S., despite McDonald's and Coca-Cola Co.'s official ties to the soccer extravaganza. And those are just two examples among many.

Such debacles won't be repeated in 1996 if ACOG can help it. A full-time sponsor-protection director and staff of 30 will monitor ads and merchandise for piggybacking. They'll respond to ambushers directly, take out name-calling ads in newspapers, and sue if necessary. One dummy ad begins: "XYZ Corp. is intentionally misleading the American public...." A second juxtaposes a sponsor's logo with an ambusher's, one under the rubric "Hero," the other under "Villain." The ads, which will dis-

than \$200 million on its homeotages. That includes around \$50 million on an attraction near Olympic Park and millions more on a pin-trading center, billboards, and production of an Olympics-related TV program. Hospitals during the games could cost the soft drink gargantua upwards of \$25 million. TV spots will nick an additional \$60 million.

Coke expects to get its money worth. "It's imperative to us at Coca-Cola to pay off our investment in the Olympics before the opening ceremonies," says Stu Cross, Coke's director of worldwide sports marketing. "We're trying to get in earlier and do more

GOING FOR THE GOLD RIGHT NOW

COCA-COLA Olympic Park attraction, torch run, ticket promotion under way. Already booked more than \$60 million in TV time during games.

HOME DEPOT Sponsoring Olympic brick program to build store traffic. But slow brick sales led to shifting promotion displays from some store entrances.

IBM Building games' information infrastructure. Already showcasing its Olympics expertise for clients with complex, time-sensitive computer needs.

JOHN HANCOCK Sponsors pre-Olympic events, then tries to sell policies to participants' families. Using Olympic getaways as employee sales incentive.

NATIONSBANK Produced expensive video to rally employees. Already using sponsorship in ads.

SENSORMATIC Security firm is using sponsorship to make its name among prospective clients. Employee sales program already in place.

DATA BUSINESS WEEK

tinctly spell out ACOG's beef with ambushers, will run within 48 hours of any offense. "We've got a fast-response mechanism in place," says William McCahan, chief marketing officer for Atlanta Centennial Olympic Properties.

Olympic sponsorships have been controversial investments since 1928, when Coca-Cola Co. loaded 1,000 cases of Coke on the U.S. Olympic team's freighter to Amsterdam. Today, the financial stakes are many times higher, and the \$40 million top sponsorship fee is just a start. Coke may spend more

cause the sponsorship costs a higher." In coming weeks, Coke will announce major worldwide promotions. It is expected to drop \$12 million or so to sponsor the Olympic torch relay. In addition, it will be prime source of ticket information via leaflets packed in with Coca-Cola products.

SMALL FRY, TOO. To be effective, a sponsor's hype must go well beyond using the Olympic rings in ads. NationsBank Corp. produced an inspirational ode by filmmaker B. Greenspan: It equates Olympic ideals with those of the bank, and nearly every employee has seen it. IBM hopes to parlay its expertise managing the games' olympian computer systems into an effective sales tool. John Hancock Mutual Life Insurance Co. sponsors pre-Olympic boxing, swimming, and gymnastics meets, then makes sales calls to contestants' families.

For smaller fry, an Olympic sponsorship offers a chance to play referee to marketing's whale sharks. Consider Sensormatic Electronics Corp. The little-known company will handle security at the games. It's no coincidence that it will soon host a meeting on security for sponsors at its headquarters in Deerfield Beach, Fla. "When we have them here, we're obviously going to take advantage of the showroom on our premises," says

Louis Chiera, director of Olympic marketing for Sensormatic.

Such efforts can help even apparent profligates get their money's worth from a sponsorship buy, if they move fast. "The Olympics can pay off," says Jim Andrews, editorial vice-president of the *IEG Sponsorship Report* newsletter. "The Atlanta Olympics are the next big worldwide sporting event. You have to build up to it, build the hype." For the 1996 Olympic hype-building event, the starting gun has already been fired.

By David Greising in Atlanta

GLOBAL WARMING: THE DEBATE HEATS UP

Are tougher CO₂ limits needed? The data are inconclusive

John B. Shlaes is on red alert. As executive director of the Global Climate Coalition, a 55-member U.S. business group that lobbies influence policy on climate change, he sees an imminent threat. In March, delegates from 118 nations are set to meet in Berlin for the most important conference on global warming since the Rio Summit in 1992, when they signed a global treaty to stave off climate change. Now, some nations want to amend the treaty to include steeper cuts in emissions of carbon dioxide and, perhaps, more far-reaching measures. "Some of these things could get passed," warns Shlaes. If so, "they put the U.S. at a competitive disadvantage."

The global-warming hawks led by 36 island states in the South Pacific, Indian Ocean, and Caribbean, which could be threatened by the rising sea levels that may accompany any warming. The 11-month-old treaty initially called for industrial nations to cut emissions of greenhouse gases voluntarily to 1990 levels by 2000. But hawks have proposed that industrial nations, which spew out 48% of the world's CO₂, reduce emissions an additional 20% beyond 1990 levels by 2005.

Other measures put forth by various European countries, especially those likely to meet their goals, include imposing formal targets and timetables for emissions reductions that end beyond 2000 and setting international standards for technology.

The hawks argue that the more stringent measures are necessary because the current provisions are inadequate. Last year, the Intergovernmental Panel on Climate Change (IPCC), the body that evaluates global-warming research, an-

officials reported that 9 out of 15 industrial countries, including the U.S., which had submitted plans to cut emissions under the current treaty, weren't going to meet their goals. In fact, Japan estimates that by 2000 its emissions will be 3.1% higher.

Tougher measures, however, even if ratified, may have little immediate impact. "Until industrial nations meet their current goals, more ambitious programs are sure to fail," says one Chinese official. China, India, and Saudi Arabia will be among the nations opposing stricter emissions standards. Moreover, since only 18 out of 36 industrial countries have filed their plans for cuts, policymakers don't have enough data to move forward, say others. Then there's the cost: No one has studied the economic

impact of a 20% cut, although a 1992 Stanford University study did conclude that the faster emissions cuts are made, the more expensive they will be.

"FINGERPRINTS." Even so, those calling for stricter standards say plenty of scientific evidence indicates a global warming may be under way. They cite everything from satellite-confirmed rises in sea level, recent increases in the frequency of the tropical El Niño climate systems, a rise in global temperatures of about 0.4C this century, and record high temperatures in the 1980s, which resumed last year after a three-year cooling. The recent relative change of recorded temperatures on the surface and in the atmosphere provides what James E. Hansen, head

of NASA's Goddard Institute for Space Studies in New York, calls "evidence for the fingerprints" of a global warming.

Yet Hansen and others also agree with Thomas Karl, a scientist at the

National Climatic Data Center, who says it is premature to draw conclusions. Scientists need a longer record of data such as surface land, water, and atmospheric temperatures, sea-level rises, and how much sunlight reaches the atmosphere. That, plus data on



nounced that to stabilize the cumulative amount of CO₂ in the atmosphere at even double current levels, man-made emissions would have to drop below 1990 levels. Then in February, U.N. of-

STILL LOOKING FOR THE ANSWERS

A treaty to prevent global warming is just 11 months old, yet some countries want stronger action now, including a new 20% cut in emissions—despite a lack of compelling new scientific evidence:

- Scientists don't know if recent climate changes, such as warmer temperatures, are part of a long-term trend or whether they're natural or man-made
- Climate models are becoming more sophisticated, but they can't yet reliably predict the effects of any global warming, especially regional variations
- It is likely to take at least five years to find the "smoking gun" that signals any global warming

historical climate from coral, ice cores, and tree rings, will help them to determine whether warming is a long-term trend—and if it is, whether it's caused by natural forces or by man-made gases. "We're learning to distinguish the natural changes, and we know what it takes to do the detection," says Tim P. Barnett, an expert in detecting global warming at the Scripps Institution of Oceanography. "But it's hard to justify more draconian measures based on the information we have."

Scientists are improving climate models used to predict changes. Recent research has led to a better understanding of the role clouds play in absorbing sunlight, how much CO₂ forests and oceans soak up, the cooling effect of pollution and volcanic eruptions, and historical climate. By plugging such information into the climate models, along with more recent data on greenhouse emissions, the models now predict lower potential warmings, about 2F to 4F, further into the future. Even so, predictions remain speculative, especially those involving any regional climate variations.

SMOKING GUN. Meantime, research continues to add new dimensions to the global-warming puzzle. By applying time-series analysis techniques he devised, David J. Thomson of AT&T Bell Laboratories recently found that in the middle of this century, just as CO₂ levels were taking off, the timing of the earth's seasons was disrupted—they started earlier in some places, later in others. "The data suggest that the rate of drift in the annual cycle is unprecedented and appears to be correlated to the increase in carbon dioxide," says Jeffrey J. Park, associate professor of geology and physics at Yale University.

If Thomson's work pans out, it suggests that one effect of rising CO₂ levels could be more unpredictable seasons. In any locale, the annual cycle of temperature is controlled either by the cycle of sunlight received there or the cycle of heat transported from elsewhere, the tropics, for instance. Thomson speculates that rising levels of CO₂ may disrupt the balance of those cycles.

Thomson's work is sure to kick off debate and new research. But even scientists who believe a warming is under way concede it will be at least 5 to 10 years before they find the "smoking gun" or "guns" that signal it—and enough evidence to indicate that CO₂ is the cause. Absent that ammunition, global-warming hawks are unlikely to muster enough political support for more expensive action—at least for now. But if, as some scientists predict, the mercury keeps rising, drastic measures could quickly become more politically fashionable.

By Emily T. Smith in New York

Social Issues



AFFIRMATIVE ACTION

A 'RACE-NEUTRAL' HELPING HAND?

To survive in the '90s, affirmative action may have to adapt

Pacific Gas & Electric Co. has long been a proponent of affirmative action. But these days, the San Francisco-based utility says downsizing has made it nearly impossible to meet to its minority hiring targets. "We're always playing catch-up," gripes Barbara Coull Williams, PG&E's human resources vice-president. That's why the federal contractor is asking Washington to approve a pilot program that would count mentoring and leadership-development seminars as part of its affirmative action program.

What a difference a few years can make. Through the 1980s, Big Business backed federal antibias rules because they provided a shield from discrimination suits. But today, the climate for affirmative action has changed. It's under assault in the states, Congress, and the Supreme Court. Now, even Corporate America is having second thoughts.

Some companies and policy experts are devising new ways to offer preferential treatment. The delicate task is to assuage the white backlash without igniting a black one. One option

now gaining political momentum: break based on economic need, not race or gender. "In this environment, you may have to choose between diluting the concept or losing it altogether," says Milt D. Morris, vice-president of the Joint Center for Political & Economic Studies, a black think tank in Washington.

CONFLICTING NUMBERS. The affirmative action debate is arousing emotions on all sides. And it's hard to cool feeling down with hard, cold numbers, since few exist and most of the research is inconclusive. University of Chicago economist James J. Heckman, for example, has shown that antibias laws—which don't require efforts beyond nondiscriminatory behavior—had a greater effect than affirmative action in promoting black employment. But those studies only looked at the years 1964 to 1975.

And, as usual, the few statistics are used to support both sides. By 1992, 5.3% of blacks, 3.2% of Hispanics, and 2% of Asian Americans held managerial positions, compared with less than 1% for each group in 1966, says the Equal Employment Opportunity Commission.

BEYOND QUOTAS

Employers want credit for their diversity programs, too

ponents view the jump as evidence affirmative action has helped but is needed to integrate the workforce. nents see it as proof that racial rences have done their job. Now, insist, it's time for new ideas.

ferences based on economic need both sides a compromise of sorts. on Administration officials, struggle to respond to angry white male s, are now beginning to examine lea.

needs-based system is also gaining

among the GOP moderate Demo-, who want to rve some breaks ie disadvantaged. n't want to throw aby out with the water," says Clint k, vice-president e libertarian In-e for Justice. He ping congression-epublicans draft ation that would se a needs-based em in school ad-ons, federal con-ing, and employ-. Bolick says oyers could "give s to people who overcome disntages in their

ponents say a s-based system d still benefit m-ies, who are dis-ortionately poor. critics say an ec-e test is no pana-In 1993, 20.3 mil-white households earned under 00, compared with 6.7 million black 4 million Hispanic households. d'd have an awful lot of needy es taking the place of blacks," says ail Thernstrom of the conserva-Manhattan Institute for Policy arch.

OFF POINT. Meanwhile, companies struggling to balance the interests of loyees. Instead of having the gov-ent set staffing goals, companies credit for "diversity strategies." aim to develop all employees by ing workers sensitive to each oth-diverse backgrounds.

oneywell Inc., for one, sponsors shops on employees' cultures and a review process to identify prom-candidates. It says such programs promote minorities and defuse the backlash against racial preferenc-The affirmative action process at eywell was successful up until three

years ago," says Curtis White, Honeywell's vice-president for corporate diversity. "But a plan like that cannot be put in place indefinitely."

The flaws in affirmative action have led some reformers to call for its elimination. Lawrence H. Fuchs, a professor at Brandeis University, would start by denying benefits to new immigrants because he argues they haven't suffered past discrimination in the U.S. After that, "we have to say at a date certain, all counting by race should be phased out," he says.

Charles Kamasaki, policy director of the National Council of La Raza, an Hispanic civil rights group, worries about drawing a line that defines who has suffered discrimination. He notes that a longtime U.S. permanent resident may have suffered as much bias as an African-American.

Blacks, too, have their doubts about affirmative action's success. In the long run, some think self-help may serve them better than painful integration efforts. Young African Americans are flocking to historically black colleges, where enrollment rose 25% from 1986 to 1992, compared with an overall 13.8% jump at all U.S. colleges, according to the United

Negro College Fund. White colleges "have not engaged in the wholesale recruitment, admission, and nurturing of [black] students," says Walter J. Leonard, former president of Fisk University in Nashville.

Regardless of how the debate goes, the progress of minorities and women in the workforce won't come to a halt, say executives. They're an increasing portion of the labor market. And companies need to reflect their more diverse customer base to gain a competitive edge. Even if affirmative action were repealed, "we would still need different types of people," says Susan K. Cooper, senior vice-president at Bell-South Corp. The trick for policymakers will be to map a course that will bring people together, not split them further apart.

By Catherine Yang in Washington, with Maria Mallory in Atlanta and Alice Cuneo in San Francisco

New Thinking on Affirmative Action

LIMIT BREAKS TO NEEDY

This would counter claims that affirmative action helps well-off minorities. But minorities fear being squeezed out by poor whites.

RESTRICT USE BY NEW

IMMIGRANTS Supporters argue that minorities suffering past discrimination deserve benefits more than new immigrants.

FOSTER DIVERSITY

Instead of strict head counts of women and minorities under affirmative action, companies prefer diversity strategies intended to foster a bias-free workplace.

BLACK SELF-HELP

Some African Americans prefer creating their own avenues for success—for example, all-black colleges—rather than relying on affirmative action.

DATA: BUSINESS WEEK

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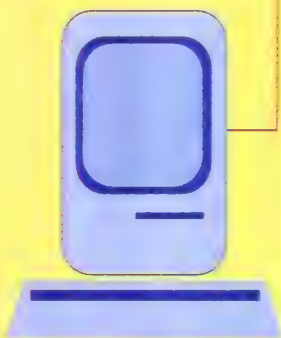
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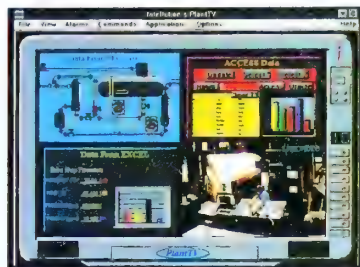
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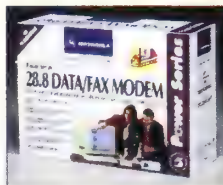
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EDITED BY AMY DUNKIN

BUOYING WOMEN INVESTORS

Debra Tarleton's first experience with a securities broker was fraught with frustration. After giving him her retirement savings to manage, the 41-year-old maternity and children's supply retailer from Charlotte, N.C., didn't hear from him for a year. She finally prevailed on his secretary to send her a statement for the mutual fund he dumped her money into. "It was a communications problem," she says. "I couldn't get satisfactory answers to all my questions I had."

INVESTING

"Women want to know that the broker is more interested in the person than just the money"

Luckily, Tarleton didn't give up. Lorraine Fiorillo, a Prudential Securities financial planner recommended by Tarleton's partner, spent an hour going over the mutual-fund statements with her—and helped her set up an individual retirement account and a self-employment pension plan for her business. The best broker "made me feel that I didn't have any money to do anything with," Tarleton recalls. "Lorraine didn't. Her philosophy is to have to start some-

where and do what you can."

As the financial-services industry has been discovering, Tarleton's experience is not unusual. Surveys show that women often get short shrift from brokers, and although women—like men—come to investing with various levels of savvy, they tend to want more individual attention and information than they have traditionally received.

MISCONCEPTIONS. Brokers and banks have a vested interest in catering to female customers. Women make up 40% of the population with assets of at least \$500,000, according to the Internal Revenue Service. They're almost 50% of the workforce, and they own 30% of the businesses. Meanwhile, many women today are grappling with the need to be self-sufficient; they can no longer count on a husband's income or pension to see them through.

Investment firms from Smith Barney to Chase Manhattan are responding by

sponsoring regular seminars in which women are encouraged to express their concerns and ask financial questions—no matter how basic. "Everyone who comes to us thinks they don't have enough money for us to be interested in them," says Ann Benson, who runs Merrill Lynch's women's investing seminars. "It's up to me to show them we're listening and responsive." Other programs offer booklets and videotapes that outline how to get your finances orga-



what the investment
s are, and how to eval-
hem.

ditionally men have re-
l more training in mon-
agement than women,
oth groups have a lot
arn. A 1992 study by
utual-fund firm Oppen-
er Management found
39% of the women sur-
l (vs. 69% of the men)
o idea what the level of
ow Jones industrial av-
was; 77% (vs. 65%)
understand the relat-
ship between interest
and bonds; and 69%
53%) didn't know that
s historically outperform
s, certificates of deposit,
money-market funds.

vestment advisers find
en often have a different
ach to finances. "Wom-
ant to know that the
er is more interested in
person than just the
y," says Alexandra
strong, a financial plan-
t Armstrong, Welch &
ntyre in Washington.
"They don't like being
individual investment
acts. They're more com-
ble being asked what
financial goals and con-
are and buying invest-
s in that context."

ey are also less likely
vest on the basis of a
tip. "Women want to
through investment de-
ns more carefully and
a good grasp of what
're buying," says Lee
t, a Prudential broker,
is part of a father-
hter team that gives in-
ment seminars to wom-
Even when his female
ts are stockpickers, he
, they tend to ask more
t the company.

PRESSURES. Unfortu-
ly many brokers don't
e the time or inclination
t down and answer lots
uestions. And perhaps
use male brokers vastly
number female brokers,
routinely solicit male cli-
more aggressively than
men. A woman in one of
enheimer's focus groups
plained that brokers still

called her house asking for
her husband, even though he
had been dead for six years.

Studies also find that
women are more risk-averse
than men. When asked what
they would do with a \$25,000
windfall, 37% of the women
respondents (vs. 27% of the
men) said they would put the
money in a CD, according to
SRI International, an indepen-
dent research firm in Menlo
Park, Calif.

Lack of female experience
with investing stems from
American cultural tradition.
Older women typically dele-
gate investment decisions to

offers to do the finances, it's
one less chore."

But the need for women
to become savvy investors is
pressing. They outlive men
by an average of five to sev-
en years, yet they still earn
and save less, drop in and
out of the workforce more,
and suffer more financially
from divorce. Over 70% of
the elderly poor are women.

Probably the easiest way
to get a grip on financial
matters is to find an adviser
you trust. Ask friends whom
they use and seek recom-
mendations from women's or-
ganizations and local broker-

Clubs such as The Beards-
town Ladies in southern Illi-
nois, whose members range
in age from 41 to 82, regular-
ly outperform the stock
market. A good resource is
the National Association of
Investors.

Whether you choose an ad-
viser, join an investment club,
or simply want to go it alone,
it's wise to study financial-
planning and investment
books on your own time. *The
Beardstown Ladies' Common
Sense Investment Guide* (Hy-
perion, \$19.95) and its com-
panion video spell out the
club's investing strategy and
how it was set up. Joel Lerner's
*Financial Planning
for the Utterly Confused*
(McGraw-Hill, \$9.95) has a
section devoted to women.
Other helpful books are Jane
Bryant Quinn's *Making the
Most of Your Money* (Simon
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dreds of investment seminars
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pendent financial planners
about working with women,
its representatives can also
make referrals. Merrill Lynch
also sponsors nationwide
seminars that feature panels
of experts on subjects such
as global investing. The Na-
tional Center for Women &
Retirement Research at
Long Island University has
numerous tapes and work-
books focusing on everything
from budgeting to long-term
health care.

Much of the material cov-
ers similar bases: determin-
ing your assets and liabil-
ities; figuring out your
financial goals and how much
you will need to achieve
them; evaluating risk; under-
standing what investment
options exist and how to
choose among them. They're
issues that lead to sound
money management—
regardless of what gender
you are.

Pam Black

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their husbands, who earn the
money, says Vickie Thomas,
who runs focus groups for
women over 50 for financial
institutions. Many of these
women face their financial in-
itiation when they are most
vulnerable—after divorce or
the death of a husband.
Younger women are often
preoccupied juggling job and
family. "A popular myth is
career women are more in-
volved in finance," says Alex-
andra Armstrong. "Particu-
larly for a married woman
with a family, if her husband

ages. If the person talks
down to you or isn't clear in
answering your questions, go
to someone else. Be wary of
advisers who are just inter-
ested in selling you products.
And be sure to look for a
financial plan that takes
your individual needs—rather
than a boilerplate formula—
into account.

Another route is to start
or join an investment group
with friends or colleagues, in
which each of you researches
companies and invests small
amounts of money at a time.

'TRAVELER'S CHECKS' GO PLASTIC

Visa International wants you to think of it as a traveler's check that looks like a credit card. Feed the new TravelMoney card into any of 200,000 Visa/Plus automated teller machines worldwide and get cash back in local currency. You say you can do that with your credit card or bank ATM card?

That's true. But TravelMoney has some features other cards lack. Known as a "stored-value" card, it is purchased from a bank at a set amount, with a service fee of about 2%—twice that for most traveler's checks. The ATM deducts value from the card as it dispenses cash, at

near-wholesale currency-translation rates. When the card is depleted, you throw it out.

Visa believes vacationers who normally use traveler's checks—partly as a way to budget a trip and avoid the temptation of credit cards—will prefer the convenience of TravelMoney. Ditto for corpo-

rate travelers who find cash-on-a-card a better way to take a cash advance.

Available now in limited markets, Visa plans a rollout for TravelMoney in June. The cards can be purchased in any amount. The card is encoded with a personal identification number selected by the buyer,

and if lost or stolen, a toll-free call will disable it; Visa promises a new card with a new PIN in 24 hours. One advantage over traveler's checks: You can buy two or more cards with sep-



arate PINs that access the same prepaid account, so if one turns up missing the other can be used immediately.

Not so fast, counters American Express, which sold \$24.9

billion worth of traveler's checks worldwide last year, up 5.5%. AmEx spokesman Toby Usnik notes that traveler's checks, which can't be replaced, are still popular. Since many merchants accept traveler's checks, you can carry little cash. He also wonders what good a TravelMoney card will do "when you

are on some island off the coast of Sri Lanka with no ATM in sight."

Similarly, MasterCard International

believes the market for stored-value cards is too limited. "We did research, but we didn't find sufficient interest," a spokeswoman says.

The market will decide who's right. For now, TravelMoney is available at First Bank System in Minneapolis, Bank of Scotland, and three Mexican banks, but Visa International expects the cards to be widely available by year-end. *Russell Mitchell*

SMART MONEY

FLEXIBLE FUNDS FOR IFfy TIMES

Plotting a fixed-income strategy has gotten a lot tougher now that

we've experienced one of the worst bear markets for bonds in history. The yield curve has flattened, and

many battered sectors are cheap, so you'll want to do more than stay in short-term bonds. But how long should you go? Should you venture into high-yield or stick with the old reliable? Slip your toes into foreign bonds or stay home?

If you'd like a professional money manager to make such decisions for you, you may want to consider a flexible or "strategic" income fund. This relatively new class of funds, usually sold by brokers with a sales load, diversifies among government, high-yield corporate, global, and other types of debt. "The basic idea makes fabulous sense," in a bond world divided into "micro-cuts" such as short-term world income and adjustable-rate mortgage funds, says Eileen Makoff, an asso-

ciate editor with Morningstar Inc.

Here, as with stocks, diversification cuts risk, since the performance of different sectors usually doesn't correspond. This wasn't the case in 1994 when fixed-income markets fell across the board. Flexible-fund sponsors had hoped portfolio managers would be able to sidestep some of the mayhem because they can adjust sector weightings to react to changing markets. But few were able to do this.

An exception is Ron

Speaker, manager of Janus Flexible Income. He kept his funds' loss to 2.92% in 1994, while income funds (including those that also invest in high-dividend stocks) on average lost 4.51%. Speaker's strategies: raising cash, shortening maturi-

ties, and using futures to hedge against rising rates.

But some managers made things worse by shifting between sectors. Phoenix Multi-Sector Fixed Income, which invests in 10 sectors of the bond market and has a laudable 10.2% five-year average return, fell 6.77% last year. Managers had bought up emerging-market debt that seemed cheap only to see those markets crash in December.

Not all funds allow as much flexibility as Phoenix and Janus. Oppenheimer Strategic Income, Putnam Diversified Income, and Smith Barney Shearson Diversified Strategic Income have investment parameters that prevent the manager from loading up on any one sector. That didn't particularly help them in 1994. But in the long run, having a diversified bond portfolio in one fund still makes sense. *Amey Stone*

Funds That Pick a Basket of Bonds

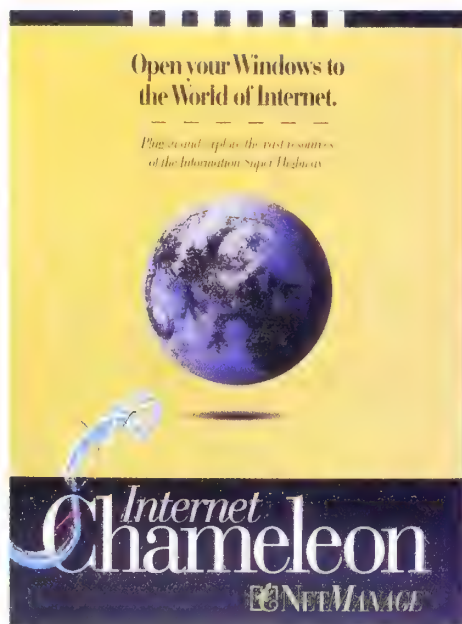
FUND	TOTAL RETURN	
	1994	3-YEAR AVG.*
BLANCHARD FLEXIBLE INCOME	-5.54%	NA
JANUS FLEXIBLE INCOME	-2.92	7.9%
OPPENHEIMER STRATEGIC INCOME	-4.7	7.06
PHOENIX MULTI-SECTOR FIXED INCOME	-6.77	6.37
PUTNAM DIVERSIFIED INCOME	-5.59	7.08

*As of 12/31/94 NA=Not available

DATA: MORNINGSTAR INC.

THE INTERNET

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A TOAST TO THE 'CAL-ITALIANS'

California's wine industry was cultivated mainly by Italian immigrant families. Yet

it has prospered on the strength of the French-style wines more familiar to consumers—primarily cabernets and chardonnays. The Napa Valley climate, however, is more like Tuscany than Bordeaux. And in the past few years, vintners have been experimenting with Italian grape varieties such as sangiovese and nebbiolo. Early offerings were uneven and sometimes overpriced. But suddenly, the category of "Cal-Italians" is bursting with high-quality new wines and refinements on earlier vintages from respected producers.

Many well-known vineyards are embracing the Cal-Italians, including Atlas Peak California Wine, Bonny Doon, Ferrari-Corono, Robert Pei, Swanson, and Viansa. Wine buffs are eagerly anticipating the May launch of La Famiglia, a new line from Napa's esteemed Robert Mondavi. In unique sculptural bottles with

elegant foil labels, Mondavi's first release will be collector-edition quantities available only at the winery. The Mondavi offerings will cost \$11 to \$20 and include sangiovese, barbera, malvasia bianca, and tocai friulano. Look for La Famiglia in fine wine shops around the country starting in '96.

This trend coincides with Americans' growing love of northern Italian cuisine, which features grilled meats,

POTABLES

fish, and lighter sauces, according to Napa-based Ron Wiegand, editor of *Restaurant Wine*. Even the red wines common to northern Italian regions, such as Chianti, are spicy and flavorful but lighter than cabernet sauvignons and so complement the region's foods. Wiegand estimates that one in eight California wineries now has an Italian-style wine or soon plans to produce them.

FAST FINISH. As usual in the wine world, the names can cause confusion. Chianti is a region in Italy, but the primary grapes that go into Chianti-style wines are sangiovese. Wines dubbed "California chiantis" have appeared over the years, but they were of varying quality and not necessarily made from sangiovese grapes. Also, some California sangiovese offerings in recent years have retailed for \$20 to \$30 yet had no advantage over \$10 true Italian Chiantis.

Several recent Cal-Italian sangioveses priced above \$20 are highly regarded, however, including Swanson and Atlas Peak Reserve.

Good midpriced Cal-Italians are appearing, too. In an informal BUSINESS WEEK tasting, Pellegrini's 1993 Barbera (which sells for about \$9 in California) won raves for being soft and full-bodied. Characteristic of that grape, it tends to "finish"

dry white wine with a spectacular bouquet of fruit fresh flowers that sells about \$8. Bonny Doon is better known for its Rhône-style wines, but malvasia is from its Cal Solo line, which also includes a Chianti-style wine called "Il fiasco"—its label shows waiter nearly upsetting tray. Mondavi's new malvasia, on the other hand, has a sweet finish and refreshing citrus flavors.

ROOT LOUSE. Until recently, very limited quantities of the wines were available, sometimes sale only at the wineries. You may need to call to find out where you can buy the wines locally—or in limited quantities, order them by mail. But lately, volumes are increasing and distribution is expanding for interesting reasons. California vineyards have been plagued with phylloxera, a root-infecting louse. "Phylloxera has spurred" the replanting of more Italian varieties of grapes, says G. Salva, vice-president at Atlas Peak. According to the Wine Institute, the volume of sangiovese grapes harvested grew from 1.7 tons in 1987 to more than 500 tons in 1992.

Some wineries are even experimenting with an Italian technique called "field blending," in which different varieties

grapes are planted in a single vineyard, then harvested together to produce a blendable wine. Variety is one of the great joys of wine—these rediscovered traditions are invigorating California producers while giving wine buffs something new to savor.

Joan Hamilt



Italian Grapes On California Labels

SANGIOVESE Lighter than cabernets, but spicy. Primary grape of Chianti.

NEBBIOLO Creates complex, smooth reds. In Italy, the foundation of Barolo wine.

BARBERA Until recently, used mainly in California to augment jug wines. Quality is improving with full-bodied reds.

PINOT GRIGIO Produces simple, clean white wines. Identical to the French Pinot Gris.

MALVASIA BIANCA Makes fragrant, low-acid white wines. They may be sweet or dry.

quickly on the tongue—reinforcing its lighter profile. More values for around \$10: nebbiolo from Martin Brothers and barberas from Louis M. Martini, which has made Italian-style wines for decades.

Bonny Doon's malvasia bianca is a bright, lively,

WORTH NOTING

■ SELF-EMPLOYMENT.

Learn about a range of entrepreneurial opportunities—from candy shops to weight loss centers—in the 1995 *Directory of Franchising Organizations*. The 80-page paperback lists more than 750 companies, with addresses, descriptions, and approximate investments required. Order from Pilot Books, 103 Cooper St., Babylon, N.Y. 11702, for \$5.95, plus \$2 for postage and handling.

TECHNOLOGY MANAGEMENT UNDER SIEGE

The 1994

BUSINESS WEEK

SRI International

Technology

Management

Symposium

The technical crown jewels: the enabling resources that can make the world's corporate technology leaders great companies. Businesses of all types recognize that better management enforces and accelerates the technology payoff. However, demand for better products delivered faster, the pace of technological change, global competition, and other factors are placing unprecedented demands upon technology managers. They are asked to deliver more and being given less to work with. In short, technology management is under siege. That is why *BUSINESS WEEK* and SRI International created a Technology Management Symposium — a forum for business and technology executives from major corporations worldwide. Made possible in part by Sun Microsystems, Inc., the meeting focused on the strategic and organizational challenges brought by technology in companies today, and the understanding of the relationship between technology and competitiveness that is required to deal with them.

Seeking Seamlessness

Seamlessness is the smooth delivery of technology from multiple providers to internal and external customers; achieving it means breaking down internal walls and creating a more fluid organization. "The task," says SRI Technology Management Practice Director, Ken Colmen, "is to build and link structure, systems, and people across the organization so they will accept change in the company's situation and direction."

"Our challenge is how to meet long-term technology needs while providing the quarterly results shareholders demand," says Jay Hassan, vice president for Strategic Business at AMP Corporation. "Technology management must anticipate change. The Chief Technology Officer must spearhead new ways of thinking. That's changing people, and that's never easy."

Technology Strategy: Competitive Weapon

Technology is a major factor that gives the technology dependent firm strategic advantages...or disadvantages. "Today's technology strategy sees many leading firms focusing resources to build stronger positions in their core technologies and on the critical enabling technologies of their products and services," says Bill Sommers, president and CEO of SRI International. "To be competitive, firms must seek greater return on technology dollars, and companies today employ a variety of sophisticated approaches to link business and technology, balancing risk and reward across a number of dimensions."

The difficulty in developing technology strategy was highlighted by Eric Schmidt, chief technology officer of Sun Microsystems. "Choosing technology strategies is akin to taking a quantum leap. You're standing on the precipice. If you don't jump you'll be left behind. If you do jump, you have to have faith and you have to be right. You have no choice but to anticipate change and make your bets. You'd better have backup strategies." Senior technology managers polled at the Symposium recog-



ERIC SCHMIDT
CHIEF TECHNOLOGY OFFICER,
SUN MICROSYSTEMS

"Choosing technology strategies is akin to taking a quantum leap. You're standing on the precipice. If you don't jump, you'll be left behind..."

nized the difficulty — only 40% of them defined their own company's technology management as "good" or better.

"Virtual" Technology Management

"The model for external technology sourcing...the "virtual" concept...is a loose grouping of players who support the company's technology needs," explains Tom Boyce, principal consultant in SRI's Technology Management Practice. "Technology delivery is coordinated across the network of internal and external sources, including suppliers of component and enabling technologies, contractors, universities, national labs, and ventures with customers and competitors."

"It certainly isn't easy to do," says Gerry Meiling, vice president and director of research at Corning. "It requires a constant effort over an extended period, a lot of communications, and a lot of trust. The key is to carefully define leadership responsibilities in the joint project, develop a clearly understood business plan, and anticipate and avoid conflict. We have a motto for partnerships at Corning; 'Imagine what we can do together.' Both parties try to keep that thought in mind throughout the partnership."

One World of Technology

Like the "virtual" concept, global acquisition of technology is also surging. Companies with technology development activities in multiple countries may focus foreign technology sourcing on support of the manufacturing and marketing they happen to be doing in the foreign region concerned. Others go beyond such "multidomesticity" and create integrated technology operations that serve the company on a worldwide basis. These activities will have their own joint ventures, consortia, and linkages to the technology marketplace.

But with the fading of borders comes problems associated with the cultural

biases and stereotypes that govern the perceptions of most people. Dr. In-Ku Kang, executive vice president of Korea's GoldStar stresses "the human side" of international technology management. "The flow of technology should be accompanied by a complementary flow of engineers as well as between the CEOs, executives, and managers." In agreement, John Morgridge, president and CEO of Cisco Systems says he spends "25% of my time partnering on a global basis."

Breaking the Siege

A diversity of tools and approaches are part of the formula for making big improvements in technology's contribution. Norman McEachron, SRI senior consultant in Technology Management, points out that while important results have been achieved, companies typically undertake change from multiple perspectives without a proper framework for integrating all of their technology-delivery activities. In most companies, comprehensive frameworks for managing technical contributions to corporate success are at best in a gestation stage. How can companies best leverage their technology resources?

Stan Morris, vice president, technology and business development at Air Products and Chemicals, says he has applied a number of tools. "The question," says Morris, "was how to put them into a cohesive framework." Morris describes a diagnosis the company has completed with the help of SRI in which issues for improving technology delivery are addressed in an integrated framework of "levers for change." The next step is to choose the corresponding tools and approaches to make the many changes happen as one.

Raychem founder and Chairman, Paul Cook, who was recently named chairman of SRI, says "Technology management was just as difficult when I started Raychem in the 1950s as it is today. The difference is in the nature of

using technology for competitive advantage. Under the old paradigm, technology capability gave you competitive advantage. Today, technological moxie is not enough. The winners will be those who manage their technical abilities. That means, managing in ways that enable them to anticipate and act on threats and opportunities faster and better than competitors."

Text by Daniel Brousseau, senior consultant, International

In-hall polling provided by Quick Tally International Systems of Beverly Hills, California

Design by W2 Design, Westport, CT • Wyck

MARK YOUR CALENDAR

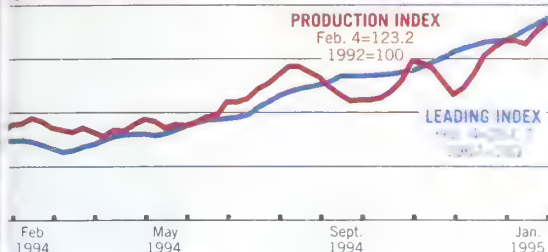
SRI's 1995 conference on technology management, *Technology Horizons: Managing Technology Fuel Growth and Drive Change*, will be held June 12&13, 1995.

SRI's David Sarnoff Research Center in Princeton, NJ. In this one-and-one-half day gathering, senior managers, technology management specialists, academicians, and policy makers will deliberate the technology questions for business competition into the next century. Critical issues such as the changing role of technology, how to compete for the technology future today, and ways to manage across internal and external boundaries will serve as departure points. In addition to expert presentation and panel sessions, conference participants and speakers will enjoy many opportunities to meet informally and share ideas. This conference is made possible, in part, by the law firm of Brobeck, Phleger & Harrison. Please contact SRI by phone (415) 859-228 or by fax (415) 859-4325 for registration or co-sponsorship information.

Business Week Index

PRODUCTION AND LEADING INDEXES

Change from last week: 0.7%
Change from last year: 8.2%



Production index rose for the week ended Feb. 4, but before calculation of four-week moving average, the index slid to 124.3, from 125.3. For January, the monthly index increased to 122.8, from 121 in December.

Leading index also rose for the latest week, and the unaveraged index at 258.6, up from a revised 257.6. For the month of January, the leading index increased sharply to 256.8, from December's 253.3.

Production index copyright 1994 by McGraw-Hill Inc.

BW leading index copyright 1994 by CIBC

PRICING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (2/10) S&P 500	480.96	472.15	2.1
GOVERNMENT BOND YIELD, Aaa (2/10)	8.28%	8.33%	17.8
INDUSTRIAL MATERIALS PRICES (2/10)	112.8	114.3r	NA*
VEHICLE SALES (2/3)	276	302	-14.6
REAL ESTATE LOANS (2/1) billions	\$414.0	\$411.8r	11.1
MONEY SUPPLY, M2 (1/30) billions	\$3,589.1	\$3,594.2r	1.5
UNEMPLOYMENT CLAIMS (1/28) thous.	326	325	-21.1

Sources: Center for International Business Cycle Research (CIBCR), Standard & Poor's, Moody's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures of companies), Federal Reserve, Labor Dept. CIBCR seasonally adjusts data on sales failures and real estate loans. *Historical data available from CIBCR.

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
MORTGAGE RATES (2/14)	5.82%	5.94%	3.25%
COMMERCIAL PAPER (2/14) 3-month	6.19	6.14	3.54
CERTIFICATES OF DEPOSIT (2/15) 3-month	6.14	6.15	3.47
1-YEAR MORTGAGE (2/10) 30-year	9.04	9.15	7.29
STABLE MORTGAGE (2/10) one-year	6.73	6.76	4.32
LIBOR (2/15)	9.00	9.00	6.00

Sources: Federal Reserve, HSH Associates, Reuters Holdings PLC

data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

FEDERAL BUDGET

Wednesday, Feb. 22 ▶ The U.S. Treasury expected to post a surplus of \$13.5 billion in January, according to the median estimate of economists surveyed by MMS International, a division of McGraw-Hill Inc. The department recorded a \$15.2 billion surplus in January, 1994. Strong economic growth is lifting tax receipts. The Clinton administration forecasts that the deficit for 1995, which began in October, will be \$192.5 billion.

FEDERAL SPENDING PLANS

Monday, Feb. 23, 8:30 a.m. ▶ The Commerce Dept.'s survey of plant and equipment spending for 1995 will probably show

that all industries are set to lift capital budgets by about 7%. That would be only slightly below the 8.8% increase planned for 1994. Beginning this year, Commerce will conduct its spending survey only twice a year, replacing its quarterly report. The revamping was done to be consistent with the department's Annual Capital Expenditures Survey. The latest spending plans will be significant because business investment is expected to be a growth leader this year.

DURABLE GOODS ORDERS

Friday, Feb. 24, 8:30 a.m. ▶ New orders taken by durable-goods manufacturers probably fell by 0.5% in January, says the MMS survey. Orders rose 3.4% in November

and 1.5% in December. A big increase in demand for military hardware boosted the December figure, however, and those orders likely were not repeated in January. The projected decline in new bookings indicates that the backlog of unfilled orders fell last month after increasing slightly for four consecutive months.

EXISTING HOME SALES

Friday, Feb. 24, 8:45 a.m. ▶ Sales of existing homes probably fell to an annual rate of 3.75 million in January. Sales have zigzagged since last summer, thanks to higher mortgage rates. In December, they rose 1.8%, to a 3.89 million pace, after slipping 2.3% in November.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (2/11) thous. of net tons	1,956	2,040#	7.9
AUTOS (2/11) units	143,356	138,043r#	3.2
TRUCKS (2/11) units	117,469	119,615r#	1.0
ELECTRIC POWER (2/11) millions of kilowatt-hrs.	NA	61,394#	NA
CRUDE-OIL REFINING (2/11) thous. of bbl./day	13,413	13,438#	0.0
COAL (2/4) thous. of net tons	22,049#	21,269	8.4
PAPERBOARD (2/4) thous. of tons	929.7#	932.0r	7.5
PAPER (2/4) thous. of tons	836.0#	836.0r	-0.7
LUMBER (2/4) millions of ft.	452.0#	476.6	-7.4
RAIL FREIGHT (2/4) billions of ton-miles	24.4#	24.0	10.9

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA¹, SFPA², Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (2/15) \$/troy oz.	376.600	374.600	-1.7
STEEL SCRAP (2/14) #1 heavy, \$/ton	144.00	144.50	3.2
COPPER (2/11) ¢/lb.	136.7	140.0	50.4
ALUMINUM (2/11) ¢/lb.	95.5	101.5	55.3
COTTON (2/11) strict low middling 1-1/16 in., ¢/lb.	87.86	89.50	22.1
OIL (2/14) \$/bbl.	18.42	18.43	32.0

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (2/15)	98.43	98.92	104.55
GERMAN MARK (2/15)	1.51	1.53	1.72
BRITISH POUND (2/15)	1.56	1.56	1.48
FRENCH FRANC (2/15)	5.24	5.30	5.84
ITALIAN LIRA (2/15)	1606.6	1617.0	1673.5
CANADIAN DOLLAR (2/15)	1.40	1.40	1.34
MEXICAN PESO (2/15) ³	5.945	5.325	3.106

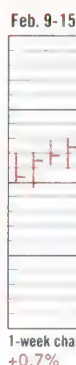
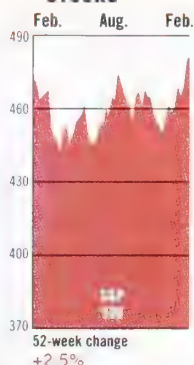
Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

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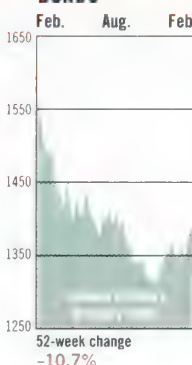
Investment Figures of the Week

MARKET COMMENTARY
 No cigar: The Dow Jones average nearly hit 4000, but profit taking set in. Dow closed at 3986, its previous record of 378 set in early 1994. Corporate profits, good news on, and a rally in the bond combined to bolster stocks. The Dow will take another step toward the millennial mark. One problem is the further down south of the border: The Dow lost an additional 10%, and stocks lost over 7%.

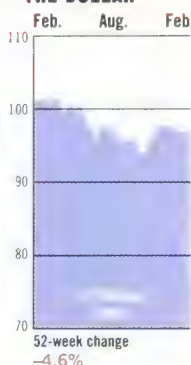
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	% change Week	% change 52-week
DOW JONES INDUSTRIALS	3986.2	1.3	1.2
COMPANIES (S&P MidCap Index)	178.8	0.9	-1.3
COMPANIES (Russell 2000)	257.5	1.5	-3.2
COMPANIES (Russell 3000)	277.7	0.8	1.5

INTERNATIONAL STOCKS	Latest	% change (local currency) Week	% change 52-week
FINANCIAL TIMES 100	3074.9	0.1	-10.0
NIKKEI INDEX	17,991.0	-1.6	-5.6
TSE COMPOSITE	4125.2	0.5	-6.8

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.88%	5.89%	3.34%
30-YEAR TREASURY BOND YIELD	7.56%	7.64%	6.46%
S&P 500 DIVIDEND YIELD	2.68%	2.69%	2.52%
S&P 500 PRICE/EARNINGS RATIO	16.2	16.4	21.7

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 200-day moving average	460.5	459.8	Positive
Stocks above 200-day moving average	52.0%	51.0%	Neutral
Speculative sentiment: Put/call ratio	0.60	0.59	Neutral
Insider sentiment: Vickers sell/buy ratio	0.76	0.84	Positive

BLOOMBERG FINANCIAL MARKETS

INDUSTRY GROUPS

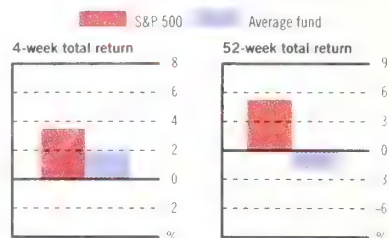
WEEK LEADERS	% change 4-week	% change 52-week	Strongest stock in group	% change 4-week	% change 52-week	Price
RESTAURANTS	13.8	8.3	MCDONALD'S	15.8	11.3	33 ⁷ / ₈
TOYS	11.4	4.7	HASBRO	13.1	-6.2	32 ³ / ₈
ENTERTAINMENT	10.3	8.0	WALT DISNEY	12.6	14.4	52 ¹ / ₂
CONSUMER ELECTRONICS	8.6	-2.8	LORAL	11.2	4.7	42 ¹ / ₈
MANUFACTURED HOUSING	8.5	-15.2	FLEETWOOD ENTERPRISES	10.8	-13.2	20 ¹ / ₂

WEEK LAGGARDS	% change 4-week	% change 52-week	Weakest stock in group	% change 4-week	% change 52-week	Price
STEEL	-9.9	-13.5	INLAND STEEL INDUSTRIES	-14.0	-15.0	29 ⁷ / ₈
CELLULAR MOBILES	-8.0	-27.5	CHRYSLER	-13.1	-22.5	45 ³ / ₈
HEAVY-DUTY TRUCKS	-7.5	-23.3	EATON	-10.8	-21.6	46 ³ / ₈
MINING	-6.8	-22.5	SANTA FE PACIFIC GOLD	-13.7	NA	10 ¹ / ₄
ALUMINUM	-6.6	5.6	ALCOA	-9.3	3.5	80 ¹ / ₈

MORNINGSTAR INC.

MUTUAL FUNDS

WEEKLY LEADERS	%	WEEKLY LAGGARDS	%
WEEK total return		Four-week total return	
WELLS FARGO CHINA & HONG KONG	10.9	WRIGHT EQUIFUND-MEXICO NATL. FID. EQTY.	-13.8
WELLS FARGO OPPORTUNITY	9.5	MORGAN STANLEY LATIN AMERICAN A	-13.8
WELLS FARGO SELECT BIOTECHNOLOGY	8.9	BT INVESTMENT LATIN AMERICAN EQUITY	-13.7
WEEK total return		52-week total return	
WELLS FARGO COMMUNICATIONS & INFORM. A	31.9	MONITREND GOLD	-53.0
WELLS FARGO SMALLER COMPANIES	28.8	TCW/DW LATIN AMERICAN GROWTH	-45.1
WELLS FARGO SELECT HEALTH CARE	28.4	FIDELITY LATIN AMERICA	-44.6



RELATIVE PORTFOLIOS

Amounts represent the value of \$10,000 invested one year ago in portfolio.

Percentages indicate daily total returns.

U.S. stocks
\$10,509
 +0.36%

Money market fund
\$10,497
 +0.25%

Foreign stocks
\$10,486
 -0.43%

Gold
\$9,896
 +0.40%

Treasury bonds
\$9,187
 -0.15%

Data on this page are as of market close Wednesday, Feb. 15, 1995, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of market close.

Market close Feb. 14. Mutual fund returns are as of Feb. 10. Relative portfolios are valued as of Feb. 14. A more detailed explanation of this page is available on request. r=revised NA=Not available

PUTTING THE PESO ON A SHORT LEASH

The time has come for Mexico to consider adopting a currency board. Despite an unprecedented \$53 billion financial aid package, the monetary credibility of the government continues to erode. The big victory of the conservative National Action Party (PAN) in Jalisco Province and the failure to capture the leader of the Chiapas rebellion are raising doubts about the political as well as economic leadership of President Ernesto Zedillo Ponce de León. His ability to enforce harsh anti-inflation policies on a restive public in the face of a sharp 40% devaluation is now being sharply questioned by the markets. The peso is weakening again, short-term interest rates on *tesobonos* are moving higher, and the *bolsa* is sinking. Weeks after the bailout was announced, the confidence necessary to revitalize private capital flows to Mexico isn't being restored. A dramatic new gesture is needed.

Enter the currency board. Argentina, Estonia, and Hong Kong have used currency boards to successfully establish effective monetary anchors to force hard domestic political decisions on economic policy and revive foreign investor confidence. Mexico should follow suit. Its central bank has zero credibility in world financial markets following disclosures that it hid the decline of reserves and the expansion of bank credit in the months before the peso devaluation.

How would a currency board work? The peso would be fixed and made fully convertible to the dollar at, say, 5¢ to 1. The monetary base (bank reserves and currency) would, in turn, be backed 100% by hard foreign currencies, mostly dollars. This would take about \$10 billion. Money could then

be created only by increasing these reserves. For every dollar generated through net exports or capital inflows, and a quarter new pesos could be generated. If Mexico added this kind of currency board, it would, in effect, be tying inflation rate and interest rates to the U.S. The Mexican government and the central bank would give up all discretionary power to pump up the money supply or to act as lender of last resort.

A Mexican currency board would broaden the economic integration that began with the North American Free Trade Agreement to include monetary policy. While the value of peso would be guaranteed vis-à-vis the dollar, internal prices would fluctuate. The PACTO, the annual agreement on wages and prices, would have to be abolished. And state-owned assets would have to be sold off to the private sector to sop excess pesos.

If all that sounds a bit like currency integration for Mexico, Canada, and the U.S., so be it. The North American Three flirted briefly with this idea during NAFTA discussions but dismissed it as politically unfeasible. A currency board for Mexico may be the next best thing. A hard-money, deflationary bias would be automatically built into Mexican economic policy. That would restore monetary credibility, encourage capital inflows, lower interest rates, and boost economic growth. Mexico has to act fast to prevent its liquidity crisis from becoming a solvency crisis for its banks and corporations. A currency board is an option of last resort. Without confidence, even \$53 billion will go pretty quickly.

MANAGED CARE BEATS MEDICARE ANY DAY

Let's hear it for markets! Health-care costs for U.S. business actually fell last year for the first time in two decades. For the naysayers who said it could never be done without heavy government intervention, the 1.1% decline is proof that competition can work miracles, even in the field of medicine. Congress should take note of Corporate America's bold medical-care overhaul and quit trying to just tinker with Medicare and Medicaid, government health-care programs for the elderly and poor.

A dramatic shift away from fee-for-service to managed care by employees of America's largest companies is behind the drop in medical-care costs. In 1994, a 21% jump in enrollment for health maintenance organizations and preferred provider organizations resulted in nearly two-thirds of all eligible employees signing on to managed-care plans. Just five years ago, health-care increases were running at nearly 20% for many big companies. Last year, for corporations employing 500 or more people, costs actually dropped 1.9%.

The same can't be said for smaller businesses. Companies with 10 to 500 employees saw their health costs rise 6.5% last

year—and very small businesses undoubtedly fared even worse. Clearly, small-business owners lack the market clout of their big-business brethren to demand lower costs for managed care. The No. 1 priority for the National Federation of Independent Business should be figuring out a way to provide health care for its members.

But even 6.5% pales in comparison to the 9%-plus annual spending hikes attributed to Medicare and Medicaid. Right now, both programs offer the most extensive—and expensive—fee-for-service options available anywhere in the country. Simply shifting people in Medicare to managed care could save as much as \$250 billion over the next seven years. Doing the same for Medicaid saves up to \$150 billion, for a total of \$400 billion. That goes a long way toward balancing the budget.

Both the Republicans and Democrats should screw up their political guts and tell those on Medicare and Medicaid that they can no longer have a medical system that is more luxurious than that of most other taxpayers. Choice is narrowing for everyone, including the elderly.

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